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ABSTRACT

The second in a two-part series, this volume presents 13 chapters discussing many of the most pressing cable policy issues facing local government, describing alternative policy options, and suggesting regulatory procedures successfully used by decision makers in the United States. Topics covered are (1) "The Rationale for Regulation," Bruce Jacobs, Nicholas P. Miller, and W. Randolf Young; (2) "State Regulation--A Current Review," Sharon A. Briley; (3) "The Franchising Process," David Owen Korte; (4) "The Cable Television Ordinance," David Owen Korte and Merry Sue Smoller; (5) "Overbuilds and Districting," John Mansell; (6) "Public Ownership of Cable," Jean Rice with "Public Ownership Models," John Mansell; (7) "Rate Regulation," Deborah Love-Heilig; (8) "Franchise Enforcement and Administration," Nancy J. Jesuale and Merry Sue Smoller; (9) "Renegotiation of Cable Television Franchises," Nancy J. Jesuale; (10) "Noncommercial Access to Cable," Nancy J. Jesuale; (11) "Leased Access to Cable," Howard J. Gan; (12) "Antitrust Issues in Cable," Howard J. Gan; and (13) "Consumer Issues in Cable," Bruce Jacobs. Appended materials include: "Actors in the Industry," Joseph W. Waz, Jr; and "Index of State Franchising Statutes," Sharon A. Briley. (LMM)

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CTIC
Cablebooks

Volume 2:
A Guide For Local Policy

Edited by Nancy Jesuale with Richard M. Neustadt and Nicholas P. Miller

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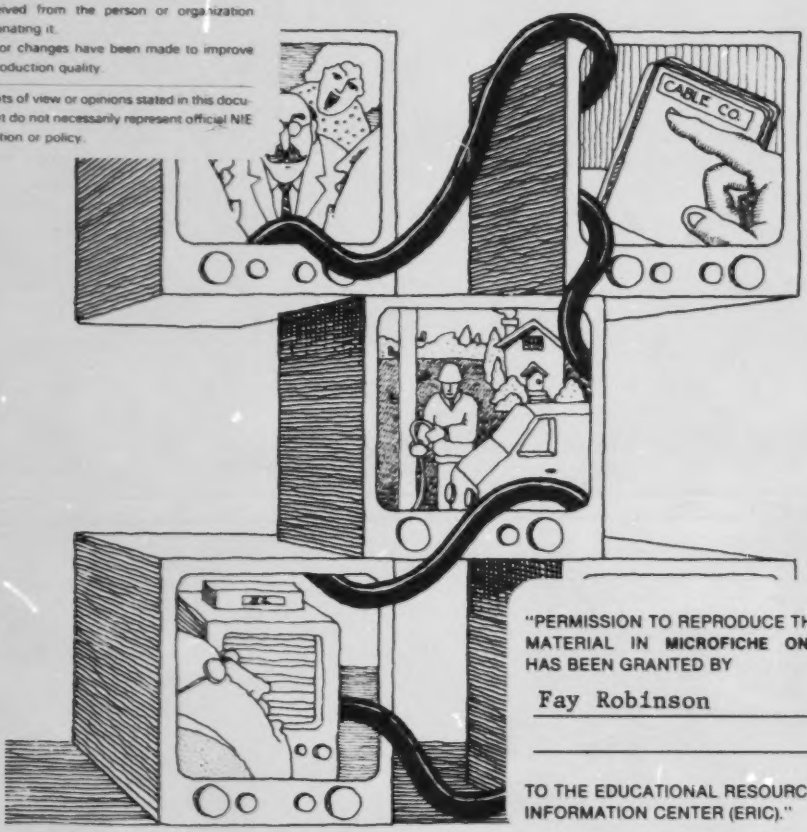

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This book evolved even as we worked on it. It was written by several authors, most of whom had no chance to see the others' work. The editors have attempted to work all of the sections into a whole that is intended to inform while remaining neutral on many issues. As such, however, there are rough spots. Even as we completed a section, a new bill or Court decision would alter the facts or our views on an issue. There are bound to be inaccuracies, especially as the volume ages, and any mistakes or inaccuracies are only the fault of the editors.

Nancy J. Jesuale

About the Authors

This volume would not have been possible without the cooperation and contributions of the 13 authors who shared their expertise in cable television policy issues. The editors gratefully acknowledge their work on this volume.

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I especially wish to acknowledge Diana Brinckman and Karen Shannon for their invaluable assistance, calm frame of mind, and confidence and support on this project. Without their work and their expertise, this volume could not have been completed.

Finally, thanks to Naomi Howe, Jamie Figuera, and Sue-Anne Wall for their work on this volume. And special appreciation to Harold Horn and Mary Milton for their confidence and assistance.

—Nancy Jesuale

This book is dedicated to Janet Quigley, Janice Sonkin Newman, and Fay Robinson who kept the Center on balance during the work on this project.

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Foreword

The need of local decisionmakers for education and information services relating to cable television has increased significantly in recent years. Two developments in the cable environment are primarily responsible for creating this need. First, the virtual explosion of available cable services—such as two-way interactive systems, institutional networks, information retrieval services, home security systems, satellite services, and access channels dedicated to community use—has multiplied the number of public service options a local government must scrutinize, both before granting a cable franchise, during the franchise period, and while the agreement is in effect. Secondly, the decreasing Federal role in cable regulation, the FCC deregulatory stance, and recent court decisions have shifted the primary burden of regulating cable to local governments themselves.

These developments have had the effect of greatly expanding the local government role in dealing with cable and have created greater public interest and involvement in the quality of a community's cable service. The impact of local involvement and the local regulatory role has been greatly increased for the local official.

The Center's experience has shown that those local governments who are most prepared are able to negotiate the most beneficial services and terms from their franchisees, as well as being better equipped to manage the franchise during its term. A badly negotiated and regulated franchise can deprive all citizens of good cable services.

The "Wiring of America" has greatly accelerated in the last 2 years. Most of the major urban areas have only recently completed the franchising process and are currently under initial construction. Hundreds of older "cabled" communities are in the process of renegotiating franchises and are expanding the local system's capacity and technical capabilities.

As energy, transportation, housing, and postal costs rise, cable will become even more of a central factor in our lives as it presents yet another option to lowering these costs and raising the standard of living in a community.

The Cable Television Information Center, which has assisted 2,500 local governments with cable related issues over the last 10 years, has attempted in these volumes to address the broad scope of questions and issues that confront a local government when formulating or reevaluating cable policy. These books are the result of our involvement with local officials who have successfully addressed the touchy issues of regulatory policies, privacy, censorship, local ownership, free ("universal") service, citizen access to the system, educational uses, and much more. It is our desire in disseminating these books to further contribute to better understanding of the impact that cable television has for local government regulators and to convey the potential impact that cable presents upon the quality of life in their communities. The *CTIC Cablebooks* were funded by a grant from the John and Mary R. Markle Foundation for this purpose.

The books are organized into two separate volumes. The first volume, *The Community Medium,* discusses cable technology and services and presents a historical perspective and a full discussion of state-of-the-art options. Volume II, *A Guide For Local Policy,* develops many of the most pressing cable policy issues facing local governments, describes alternative policy options, and suggests regulatory procedures successfully used by decisionmakers across the country. Both books contain useful appendices for reference and clarification.

We here at the Center are again indebted to the John and Mary R. Markle Foundation for their continuing assistance over our 10 year life in making an extensive series of publications available to local officials and all persons concerned with

keeping informed on this fast changing technology.

The Director of Public Information for The Cable Television Information Center, Nancy Jesuale, and the many contributing authors and editors should be proud of the contribution they have made with these two additional and very timely publications.

Harold E. Horn
President
The Cable Television Information Center

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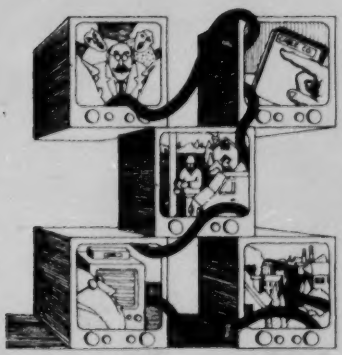

The Rationale For Regulation

Contributing Authors
Bruce Jacobs
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W. Randolf Young

Chapter 1: The Rationale for Regulation

Government regulation of cable television has been both varied and changeable. Regulation by the Federal Government, chiefly the Federal Communications Commission (FCC), has changed considerably over time. Federal regulation has gone from minimal in the 1960's to extensive in the mid-1970's and back to minimal in recent years.

State and local regulation is as varied as the number of State laws and franchise agreements. In most States, cable regulation is left to the city and county decisionmakers, who regulate through the enactment of cable television ordinances and the enforcement of franchises. But several States have enacted substantial cable regulations.

Other chapters in this volume will deal with specific aspects of State and local regulation. This chapter provides a brief discussion of the development and rationale of regulation of the cable industry as well as a description of current Federal regulation. In addition, it describes the fundamental debate over the relationship of the First Amendment to cable television, a debate that may substantially alter regulation of the industry.

Federal Regulation

Historical Perspective

Federal regulation of cable television stems from the broad constitutional authority of Congress to regulate interstate commerce. The primary statutory authority enacted by Congress is the Communications Act of 1934. This act was adopted, however, before cable television, or even broadcast television, existed. The act established the FCC to regulate radio transmission and interstate telecommunications common carriers (for example, telephone and telegraph companies). The FCC was given the broad mandate to regulate "in the public interest, convenience, and necessity."

In the early days of cable, from the late 1940's through the 1950's, the FCC made no effort to regulate the cable industry, which at that time essentially served as community antenna systems providing improved television reception in areas that did not receive good over-the-air TV signals.

As cable began to grow in popularity, however, adding new subscribers and bringing television signals by microwave from distant cities, the FCC showed an interest in the need to regulate cable. It was concerned that cable's carriage of distant television signals would decrease the audience of local broadcasters, thereby reducing the local broadcasters' advertising revenues. This, in turn, was said to undermine the FCC's broadcast policy, which is based in part on favoring local over regional or national broadcasting. These first cable regulations chiefly required that the signals of all local broadcast stations be carried by a cable operator ("must-carry" rules) and restricted the carriage of distant broadcast signals.

Although the FCC had no specific statutory authority to regulate cable under the Communications Act, the U.S. Supreme Court held that such regulations were "reasonably ancillary" to the FCC's broadcast regulatory authority.

The FCC gradually added new cable regulations throughout the late 1960's and early 1970's. Expecting that the cable industry would expand rapidly into urban areas, the Commission began requiring that operators originate programming (cablecasting) and adhere to specific technical engineering standards. The Commission also prohibited both broadcast network ownership of cable systems and broadcast station ownership of cable systems in the same market. Additional rules dealt with the local franchising process (establishing procedural requirements, limiting the length of the franchise term, and limiting the franchise fee collected by local governments) and mandating the availability of channels for public, government, and educational uses. The FCC also adopted policies governing pay cable services.

Because of a number of factors, the FCC began to reduce its regulation of the cable industry in the mid-1970's. Its cable rules received several adverse court rulings. The Commission began to believe that cable service would not significantly undermine local broadcasting, and it developed an explicit preference favoring a competitive marketplace in media services.

Currently, the FCC has few remaining Federal regulations. As this volume goes to press, the FCC still has rules for must-carry signals, nonduplication of programming, cross-ownership restrictions, application of broadcast-related rules to cablecasting (concerning issues such as providing equal time for political candidates; the Fairness Doctrine; personal attack; and a prohibition of lotteries, obscenity, and indecency) and franchise fee limitation.

In 1982, Federal regulations affect local cable service in the following ways:

- All local broadcast television signals must be available for viewing on the cable system.
- When imported distant signals carry programming already carried by a local station, the cable operator must substitute the local station signal for the imported one.
- The cable system may not be owned by a local broadcaster, local telephone company (with the possible exception of rural areas), or a television network.
- Local sports events on a distant signal that are not broadcast locally may not be shown on the local cable system.
- Most cable operators must have affirmative action programs for employment of minorities.
- Engineering must conform to minimum Federal technical standards.
- The franchise fee charged by the city may be no more than three

percent of the cable company's gross revenues unless the city can show that it needs more for cable-related purposes, in which case a fee of up to five percent may be approved by the FCC.

- Programming produced by the cable operator (origination cablecasting) for transmission over the cable system will be subject to rules similar to those for broadcasting, such as the Fairness Doctrine (which requires a balanced presentation of contrasting views), the right to reply to personal attacks, and the right of political candidates to equal time.

The FCC may modify or eliminate many of these rules. In particular, in 1982 the FCC is considering eliminating the cross-ownership restrictions on cable systems (it had already granted a waiver to one network to acquire several small cable systems), repealing the Fairness Doctrine and related broadcast-type rules for cable, and changing the limit on franchise fees.

Problem Areas

Other problems involve copyright and signal leakage. The copyright issue has long been a major area of contention between the broadcast and cable industries. Broadcasters argue that cable operators have an unfair advantage because they retransmit broadcast signals without paying the copyright royalties required of broadcasters. This debate was partially resolved by the Copyright Act of 1976, which for the first time required cable operators to make royalty payments. But the FCC's elimination of its distant signal and syndicated exclusivity rules (rules that limited the amount and type of broadcast programming that cable operators could carry) reopened the debate among the cable, broadcast, and motion picture industries, among others.

Problems of signal leakage (radio waves emanating from old or poorly constructed cable systems that interfer with broadcast transmission or radar) have emerged recently, with reports of widespread noncompliance with FCC technical standards by cable systems. Particular safety problems have emerged with Federal aviation frequencies. As a result, the FCC has stepped up its investigations and has threatened to shut down cable systems that do not comply with the FCC's technical standards.

A separate but crucial debate at the Federal level is whether to characterize cable as a broadcast or common carrier service for regulatory purposes. As technology steadily increases the capacity of cable systems and provides them with the ability to offer many different services in addition to traditional television programming, subscribers and users argue that cable systems should be viewed as common carriers rather than as adjuncts to broadcasting. This issue is discussed in more detail in the following paragraphs.

The Federal-State Relationship

Cable television has been held by the courts to be involved in interstate communications and, thus, subject to Federal control. Although it

could do so, the FCC has not attempted to preempt all State and local regulation. However, it does preempt State and local regulation in all areas covered by FCC rules, such as technical standards, franchise fees, rate regulation of pay cable services, and signal carriage requirements. For example, a local franchising authority cannot impose a franchise fee greater than the three percent of gross revenues (or five percent with special FCC permission) or require deletion of must-carry signals. A local government may not set rates for pay services, although it may regulate rates charged for basic cable services. In other areas, such as the length of the franchise term or procedures for handling customer complaints, State and local regulators can act freely in the absence of superseding Federal regulation.

The Policy Context

Ownership and Control of the System

Cable systems are typically owned and operated by profit-making corporations. Because a cable system is highly capital-intensive and subject to some risk, investors require a reasonable rate of return on their investment consistent with the risks involved. As a rule, however, a community will not have more than one cable distribution system competing for the same subscribers. Cable systems are generally viewed as natural monopolies because the system built first normally experiences substantial economies of scope and scale that preclude a second system from competing successfully for the same subscribers. Moreover, cable systems need utility-like access to public rights-of-way for aerial or underground cables or ducts.

Because of these characteristics, cable systems generally receive a local government franchise that grants them the right to use public rights-of-way in return for certain promises to serve the local community. Most franchises are by their terms nonexclusive. In practice, they operate as exclusive rights because the distribution system is a natural monopoly. The cable operator normally agrees to limitations and controls (for example, rate regulation and specified service criteria) that are not normally imposed by municipalities on other local businesses. The franchise effectively becomes a contractual agreement between the local government and the cable operator that spells out the rights and obligations of each.

A major purpose of the franchise is to protect the rights of the subscribers because the subscribers typically have no alternative supplier in the event they are dissatisfied with service. The only other way subscribers can express dissatisfaction is by cancelling service, an unattractive alternative in most instances. The competitive bid process allows a franchising authority to protect subscribers' rights by comparing alternative cable service proposals to insure that the company receiving the franchise is the one which has promised to meet the community's service needs in the most cost-effective way.

The cable operator has traditionally determined or selected the content of all programming services provided on the cable system, subject to

the general FCC rules concerning broadcast signal carriage and cablecasting and to any voluntary contractual commitment in the franchise (for example, a promise to provide certain specific pay TV signals or to set aside a certain number of system channels for public access or leased use). Where the cable operator does provide a channel for others to use, the operator may, under the terms of the franchise, or under the terms of the contract with the channel user, or under specific constitutional protections of the rights of free speech, have to relinquish control of the content of those channels (except for some limited residual rights to prohibit system use for unlawful purposes, such as the transmission of illegal gambling information).

Models of Regulation

Two basic regulatory models apply to cable. One is the broadcast model, in which the licensee (or operator) is given exclusive use of the transmission medium and complete control of the information carried over that medium. In return, the licensee is a "public trustee" of the medium and is held legally responsible for its appropriate use as well as for serving the information needs of the community. Also, the general public is allowed to receive this broadcast material without any special permission.

The other is the common carrier model. A common carrier, unlike a broadcaster, is not responsible for and cannot control the content of the information transmitted over its facilities. In essence, the carrier provides the "pipeline" and a third party provides the information transmitted over the pipeline. Moreover, persons not intended to receive the information transmitted are not entitled to receive it.

In its early days, when cable was used solely to carry broadcast signals, there was little doubt that cable operated as a broadcast ancillary service. In effect, it enhanced broadcast signals and extended them into unused areas, much as a television translator station retransmits the signal of the originating broadcast station so that it can be viewed by more people over a greater area. Later, cable's service character began to change as distant broadcast station signals were relayed by microwave into the community from hundreds of miles away. Still later, cable added the great variety of signals, both broadcast and nonbroadcast, available through satellite services. The equation became more complicated as cable operators began to originate local programming (origination cablecasting) and to provide community groups, individuals, and businesses selected use of the cable system for free (access) and for pay (leased). The final evolutionary step has been a variety of special services, many of which are subscriber interactive or two-way (for example, security alarm, meter reading, and teletext services), in which the cable operator normally does little except provide a channel to the business user to reach the cable subscriber.

Thus, a modern cable system can provide a wide variety of services and perform many functions. Individual services on a cable system compare to services available either from broadcasting or from common carriers. But

cable as a whole does not fit either of these established regulatory models.

For instance, when carrying "must-carry" TV signals, the cable operator functions much as a common carrier because it cannot select the signals and has no control over their content. Similarly, when providing access or leased channel services or a pure point-to-point communications service (for example, data or voice transmission), the operator also functions as a carrier, without control over content.

When the operator provides origination cablecasting, it functions as a broadcaster, with full control and responsibility for signal content. Indeed, as discussed earlier, the FCC applies essentially the same regulations (such as the Fairness Doctrine) for such services as it does for broadcasters.

Other cable operator functions do not fit either the broadcast or the common carrier model. These functions primarily involve selecting of services the system will carry without control over their content. For instance, the operator may select one or more distant broadcast signals or nonbroadcast programming services available from satellite.

Conflicting Views on Regulation

The extent to which governments may regulate cable is limited to a significant degree by the First Amendment, which safeguards freedom of speech and freedom of the press from government interference. For instance, the First Amendment prevents a government entity from censoring cable programming for political purposes. It is not clear, however, what other kinds of regulation the First Amendment can be said to prohibit or limit. The Supreme Court has never directly addressed the relationship between cable regulation and the First Amendment. In *Midwest Video v. FCC*, 440 U.S. 689 (1979), the Supreme Court overturned FCC regulations mandating access without discussing the constitutional issue, except to add rather cryptically in a footnote that the issue was "not frivolous."

This fundamental issue of the relationship between the First Amendment and cable regulation has been the subject of debate between the National Cable Television Association (NCTA), the representative of the cable industry, which advocates "full First Amendment rights" for cable operators; and the National League of Cities (NLC), which expresses the concerns of local governments and others and advocates that cable systems have less than an absolute freedom from regulation under the First Amendment.

NCTA argues that cable operators should be treated the same as newspapers for First Amendment purposes. Under the Constitution, newspapers have near absolute freedom of discretion as to what they do or do not publish. NCTA points out that cable operators are required by Federal regulation to conform to broadcast-type rules for cablecasting and frequently are required by State and local franchises to provide various forms of access or leased channels to third parties.

NCTA challenges the constitutionality of broadcast-type regulation

when applied to cable systems, which it characterizes as "electronic newspapers." Although the courts have upheld these regulations for broadcasters, NCTA argues that broadcasters are different from cable operators because broadcasters enjoy an oligopoly over a limited number of broadcast channels in a community. A cable system does not have the problem of spectrum scarcity that confronts broadcasters.

In direct contrast to the NCTA view of the cable operator as newspaper editor, the NLC offers its "functional analysis" of cable operations. The NLC depicts cable operators as having no control over most programming on a cable system, exercising only a broad selection authority in others, and having complete control of only relatively few programs in origination cablecasting. On those channels dedicated to access programming and must-carry signals, the operator has no right to control content. As to other broadcast stations, satellite-delivered programming, and electronic information services, the operator may select from among competing offerings but, in the NLC's view, the operator has no editorial control over the content after the service is selected. In fact, the selection itself is normally based on a business judgment to maximize profits, and not on an editorial judgment in the ordinary sense. Only when a cable operator offers local program origination does it have complete content control over its channels, according to the NLC.

The NLC contends that regulation of cable is justifiably free of First Amendment concerns whenever the cable operator is not exercising editorial judgment. Appropriate regulation of origination cablecasting, where the cable operator does not exercise some editorial control, is justifiable under the First Amendment, the NLC believes, because cable operators, like broadcasters, use a scarce public resource (rights-of-way) and could not operate without government licensing. This scarcity warrants a "public trustee" treatment of the cable operator and should permit some limited content regulation of origination cablecasting.

Aside from First Amendment concerns, local governments justify much of their regulation of cable operators on the assumption that cable is a natural monopoly. Industry advocates also challenge this notion, asserting that cable is just one of many sources of news, information, and entertainment. Among the alternatives are traditional over-the-air broadcasting, subscription television, live sports, movie theaters, video cassettes, direct broadcast satellites, and low-power television. NCTA expects competition in the nonvideo, nonentertainment areas to come from newspapers and telephone companies. NCTA further asserts that cable cannot be seen as a public utility, like telephones or water, inasmuch as cable is "nonessential" and consumer demand is price responsive, decreasing sharply as prices increase. If cable is neither a monopoly nor a public utility, NCTA argues that the pursuit of program competition is better left to the marketplace than to government regulation.

In response, the NLC argues that cable is indeed a monopoly.

Normally, two cable systems do not compete to serve the same subscribers in a community. As more and more services turn to cable transmission to reach subscribers as the cheapest alternative for a delivery system, cable operators will be able to charge more for their services than the cost the cable operator sustains. This "monopoly pest" will grow over time as more services gravitate toward cable and subscribers have no real alternative to cable if they wish to receive the services available only through the cable system. No other technology provides the same large telecommunications service capacity as a cable system. Other technologies, many of them as yet undeveloped, may, according to the NLC, provide competition to cable for one or two specific services, but none will provide the same range of services at the same time as cable. The NLC is also concerned that concentration of ownership in the cable industry will continue, as single operators control access to one community's entire multichannel system and as large horizontally and vertically integrated companies extend control over many cable systems and programming sources.

Perhaps of greater importance to NCTA than government regulations, however, are the access or leased channel requirements that are usually written into franchise agreements. These requirements mandate that cable operators make available channel capacity to various third parties that can be used to provide services competitive to the cable operator's own services. NCTA fears the cable operator will be viewed for legal purposes as a common carrier. Imposition of common carrier status would be harmful, according to NCTA, because it would reduce cable's potential profitability and discourage investment. NCTA also asserts that mandating access goes beyond the kinds of regulation necessary to exercise a municipality's "police powers" and that franchise agreements requiring cable operators to provide access were frequently forced on cable companies. As such, NCTA argues such requirements are unenforceable waivers of the cable companies' First Amendment rights.

In response, the NLC argues that mandatory access is a means of assuring diversity of voices and the offering of competitive services within a community and over the cable system. Although the cable distribution plant may be a natural monopoly, there is no reason why the cable operator should have a monopoly over the programming and services provided over the cable facility. Moreover, the NLC asserts that cable operators are not "forced" to offer access channels but do so freely in the competitive bidding process, expanding their commitments far beyond local government requirements. A cable company does not give up any constitutional right by consenting to provide access to the system by third parties.

If NCTA's views of absolute First Amendment rights ultimately prevail, most Federal, State, and local regulations would be of questionable constitutionality because they typically affect in one way or another the cable operator's discretion to choose the services available to subscribers.

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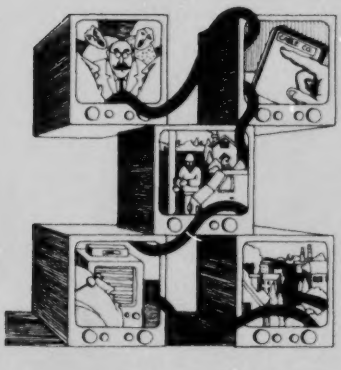

State Regulation: A Current Review

*By**
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*The views expressed are those of the author and do not necessarily reflect the views of the Federal Communications Commission.

Chapter 2: State Regulation: A Current Review

State approaches to cable vary widely. While some States have deregulated substantially in recent years, others have imposed new requirements. Major topics of current interest include local franchising authority, taxation, rates, access, ownership, program content, extension of service, pole attachment, privacy, and theft of service. The U.S. Supreme Court's *City of Boulder* decision, discussed in chapter 11, is prompting increased interest in cable activities in many State legislatures. This chapter outlines major areas of State involvement in cable policy.

The Regulating States

Since 1974, eleven States have regulated cable television on a comprehensive basis through State agencies: Alaska, Connecticut, Delaware, Hawaii, Massachusetts, Minnesota, Nevada, New Jersey, New York, Rhode Island, and Vermont. (These are usually called the "regulating states.") Six of these States—Connecticut, Nevada, Rhode Island, Vermont, Hawaii, and Alaska—preempt all local franchising authority and assign all cable responsibility to the State utility commissions, with the exception of Hawaii, where authority rests with the Director of Regulatory Agencies. Delaware applies a unique, partial regulatory approach—where the State utility commission acts in a franchising capacity only for county areas, and municipalities retain their franchising authority.

Franchising Authority

Local governments usually derive their franchising authority from the State through one of three types of legislative grants. Many municipalities franchise cable television systems on the basis of authority granted to home rule cities and counties by legislative action. In a few States, a second type of grant explicitly authorizes a city or county to franchise cable systems either in the charter or in a special legislative act. The third and most common form of grant is a general State statute specifying that a local governing body may franchise cable companies. Appendix 2 contains a State-by-State index of existing State statutory authority on franchising.

Chapter 12 discusses the concept of municipal immunity and the *City of Boulder* decision in detail. It is important to note that any antitrust immunity a municipality enjoys in its cable franchise/regulatory program is likely to be attributable to explicit language in the State statute granting the city authority to franchise cable companies. Most cities can probably presume that they lack immunity unless their authorizing statute conforms to the standards discussed in chapter 12.

Legislators in 1981-82 sessions introduced bills intended to provide antitrust immunity to political subdivisions in Colorado (H.B. 1258), Virginia (S.B. 425), Maryland (H. 1280), and Illinois (S.B. 1227); the

Interim Committee on Political Subdivisions in North Dakota considered the issue.

Franchise and Other State Fees

Financial support for most of the State regulatory programs comes from the industry itself in the form of State fee assessments. Most State fee assessments have declined from their original amounts due to rising revenues but stable regulatory budgets. For example, in New York the State assessments declined from two percent in 1973 to less than one-half percent today, and in Hawaii they decreased from five percent in 1970 to a current one percent. The State fee of one percent in Minnesota also fell—to zero—following the State Supreme Court's ruling in February 1980 that the State fee was unconstitutional.

Most franchise fees are negotiated in local franchise agreements, but several States have acted to limit local fees through statutory amendments. In 1968, California, the first State to take such action, adopted a limit of five percent on local franchise fees. The Louisiana legislature followed in 1980, limiting local fees to three percent of gross revenues but providing that "if actual cable television regulatory expenses require additional revenues, an additional commission not to exceed two percent may be charged after a public hearing." 1980 *La. Acts* 793. Current pending legislation in Arizona (H.B. 2383) would limit the fee in the same manner.

Rates

Rate regulation is perhaps the key issue for most States and local franchising authorities. The utility commissions in the regulating States set rates for basic service,[1] except in Alaska, where most systems are exempted. Most of these States apply a modified rate of return method; the New Jersey Office of Cable Television, however, has applied a common tariff approach, separating cable systems into several classes based on size and location and allowing rates to rise automatically to certain levels within each class.

Cable rates are regulated on a rate-of-return, cost-based approach in Connecticut. The Department of Public Utility Control (DPUC) defines cable companies as public utilities and requires them to file tariffs. In several recent rate cases, the DPUC directed companies whose tariff proposals included free service to public buildings not to include these costs as an operating expense in the rate base. The companies had filed tariffs on the grounds that it represented good community relations. A pending legislative proposal (S.B. 434) would permit cable companies to provide such services on a free basis.

Rate deregulation has grown in popularity in recent years. In 1980,

[1]Regulation of rates and content of pay cable services is preempted by the Federal Communications Commission (FCC).

the Massachusetts Cable Commission became the first agency in a regulating State to take rate deregulation action, basing its new policy on the presence of competitive services; that is, the availability of at least three over-the-air television signals. In the same year, and on a similar basis, the Alaska legislature exempted most systems from rate as well as most other State regulation. In New York, the State Cable Commission has deregulated its rate appeals process and pending legislation (S. 5530/A.7536) proposes to deregulate rates on a local level. The Delaware Public Service Commission in January 1982, however, issued an order that required cable companies to file tariffs (Delaware PSC Docket 81-28). Cable companies in the state had questioned the PSC's jurisdiction to take such action. A pending bill (S.B. 16) proposes to clarify the State's authority.

Rate deregulation has also occurred in nonregulating States. For example, the California legislature is currently considering strengthening its 1979 legislation (A.B. 699) that allows deregulation of cable rates on the condition that community service channels be provided. A pending bill (A.B. 2321) provides that neither cities nor cable companies may waive the provisions of the State law. Extension of the 1983 sunset provision on the present law is also under consideration. According to the California Public Broadcasting Commission, which is evaluating A.B. 699, 16 cable companies have opted to deregulate rates according to the State law's provisions. Many others have reached agreements with local governments to set their own rate deregulation policies.

Ownership

In most cases, States let local municipalities decide ownership issues through the franchising process. The regulating States that limit ownership are Connecticut, Massachusetts, and Rhode Island. The Connecticut DPUC issues decisions on an *ad hoc* basis; for example, it issued a decision on March 7, 1980 (Docket No. 791003) that prevented the Times Mirror Company from owning both the daily newspaper and cable franchises in the same community. The Massachusetts statute specifically prohibits newspaper-cable cross-ownership in a "major circulation area."

On December 11, 1981, the Minnesota Cable Communications Board repealed its newspaper-cable cross-ownership restriction on the grounds that the franchising decision occurs in a public proceeding and the existing leased access requirements in the State regulations will provide access to others who desire channels for news purposes. Pending legislation (S.F. 1570) would reinstitute the prohibition on newspaper-cable cross-ownership.

Some State laws specifically permit certain types of ownership, such as municipal ownership (Maine), municipal lighting plants (Massachusetts), and rural telephone cooperatives (Montana). A pending bill in Nebraska (L.D. 731) would authorize public power districts, municipalities, and certain municipal agencies to own and operate cable television systems. On the

other hand, some State laws prohibit certain forms of ownership. For example, pending legislation in Arizona (H.B. 2383) would prohibit municipal corporations and counties from owning a cable or any other pay television system.

Program Content

Most States have statutes barring "obscene" material from the media. A Utah bill (S.B. 301), adopted in 1981, went further and banned "indecent" material on cable systems, but a Federal district court judge declared the statute unconstitutional on grounds that its vagueness amounted to a violation of the First and Fourteenth Amendments. Legislatures in Georgia and Oklahoma also enacted obscenity laws in 1981, but similar proposals in Florida, Massachusetts, and New York did not pass.

Several proposals on program content are pending in 1982 legislative sessions. A Missouri bill provides that the promotion of pornography on cable television constitutes a misdemeanor. A Florida proposal sets similar penalties for presenting "X" or "R" rated movies during certain hours. In New Jersey, A. 912 is intended to prohibit transmission of obscene material by cable television systems. Among several bills in New York proposing remedies to offensive programming content is a proposal authorizing municipalities to impose restrictions on obscene cable programming (A. 9356).

Some States are considering a different sort of program content law intended to protect cable operators against control or censorship and place liability on the program producer (Arizona H.B. 2383 and Massachusetts S. 422).

Privacy

The issue of privacy has gained considerable State legislative attention in the past year. Illinois passed a privacy act in 1981 that covers any company that provides information or entertainment through electronic means to a household. The statute prohibits (a) the use of equipment to observe or listen to individuals in their homes; (b) provision of lists of subscribers to any person or organization, unless the company first notifies and obtains the consent of the subscriber; (c) disclosure of the television viewing habits of any subscriber without the subscriber's consent; and (d) installation or maintenance of a home-protection scanning device in a dwelling without the written consent of the occupant. The penalty for each violation of these provisions is a maximum fine of $10,000. Comparable privacy legislation is being debated due to pending legislation in Massachusetts (S. 370), Missouri (H. 1294), and New York (S. 8765/A. 11052 and A. 9848).

A State law and regulation in Minnesota is apparently the first such cable privacy provision. It states that no signals of a Class IV (two-way)

cable communications channel may be transmitted for purposes of monitoring individual viewing patterns or practices without the express written permission of the subscriber.

Pole Attachment

Disputes and negotiations on rates, terms, and conditions for cable company use of poles owned by telephone and electric utilities are underway throughout the country. To date, 21 States and one territory have certified to the FCC, pursuant to a 1978 Federal law, that they have acceptable procedures to regulate the rates for use of utility poles. They are Alaska, California, Connecticut, Hawaii, Illinois, Kentucky, Louisiana, Massachusetts, Michigan, Nebraska, Nevada, New Jersey, New York, Ohio, Oregon, Pennsylvania, Puerto Rico, Tennessee, Utah, Vermont, Washington, and Wisconsin.[2] The FCC handles disputes elsewhere. Legislation granting jurisdiction to State utility commissions is pending in Idaho (S.B. 1287), Minnesota (S.F. 364), and Missouri (H. 1466).

Access and Channel Use

Most public, leased, or other types of access requirements for cable are contained in local franchises. Several States, however, also place such requirements on cable operators. Existing regulations in Minnesota and Rhode Island and proposed regulations in New York establish minimum access requirements. In Minnesota, the first State to adopt access standards, the regulations prescribe access channels for three classes of systems, based on the population of the franchise area and the size of the system. Franchisees are also required to establish rules for administering specially designated access channels.

In 1980 the Connecticut legislature adopted a requirement that at least one specially designated, noncommercial public access channel be available on a first-come, nondiscriminatory basis. This requirement was not in effect as of April 1982.

As noted in the rate regulation section above, the 1979 California law was designed to reward the provision of community service channels with deregulation of rates.

Service Extension and Interconnection

All of the regulating States are concerned in general with the quality and extension of service. Connecticut, New York, and Vermont have service extension regulations. In several cases the States have issued decisions requiring a cable company to extend service to unserved potential subscribers in a franchised community. Connecticut's policy requires cable companies to extend service based on a certain household density formula

[2]FCC Public Notice, Feb. 2, 1982.

and potential subscribers to pay a "contribution-in-aid" percentage of the cost of construction.

Interconnection among different cable systems to allow program and service exchanges is mandated by State law in Minnesota and New Jersey. New York has studied the topic. Interconnection also is required in many local franchises. Regardless of State or local requirements, an increasing number of cable companies are entering into interconnection arrangements for the purpose of sharing programming and headend costs.

Theft of Service

Most State statutes contain laws providing penalties for the fraudulent reception of cable television service. In 24 States, these laws specifically address cable television. Most of these laws charge the user with the violation, which is usually classified as a misdemeanor in the criminal statutes. In four of these States, the theft of service laws also prohibit the sale or distribution of equipment, such as decoders. In another 27 States, the laws applying generally to theft of telecommunications services are interpreted to include theft of cable television services.

New State Studies and Legislative Proposals

Studies of cable television are being conducted in many different forums and formats. For example, Florida has a governor's task force study, and the California legislature held hearings to consider franchising, renewal, rate regulation, and theft-of-service issues. Several legislative commissions and offices in New York are actively involved with cable issues, including the Legislative Commission on Expenditure Review, the New York State Legislative Commission on Science and Technology, the Governmental Operations Committee, and the New York Office of Development Planning.

The State Corporation Commission in Oklahoma and the Public Service Commission in West Virginia are studying State regulation issues. In Missouri, a resolution proposes a Joint House and Senate Interim Committee to study the pending cable bills.

Pending bills introduced in 1982 sessions in California (A. 2742), Hawaii (S.B. 1581), Missouri (H. 1486), Washington (S.B. 4700), and Wisconsin (S.B. 665) each propose comprehensive regulation of cable under State public utility commission jurisdiction. Among the regulating States, a Minnesota bill (S.F. 518) would deregulate by gradually exempting systems with fewer than 1,000 subscribers from State regulation.

State versus Local Regulation

Debate on comprehensive State regulation versus local control, or a combination of local and State governmental control, has been on the list of cable issues for at least twenty years. Traditionally, proponents of

municipal control have argued that local rather than State officials are more suited to dealing with problems of businesses in their own communities and responding to local needs. On the other hand, advocates of State control have argued that the State is more capable of providing technical resources and assistance to localities.

Given that local governments derive their powers from the States, States are inherently involved in local decisionmaking. Municipal requests for State legislation conferring antitrust immunity in the wake of *City of Boulder* exemplify that relationship. Likewise, a complete review demands consideration of State activities within the context of Federal statutes and proposals (described elsewhere in this book). Both Federal and individual State cable television regulatory experiences should be useful to anyone evaluating advantages and disadvantages of State regulation.

Although State activity in cable television matters has increased during the past decade, that activity is not reflected in more comprehensive State regulation, but in a greater number of State statutes directed to specific matters such as franchising, pole attachment, theft of service, rate regulation, taxation, etc. There are several general causes for the lack of more comprehensive State regulation. First, although a few such bills are proposed each year, these bills are more complex and controversial than most others. Second, stronger interest groups have developed to contest "undesirable" legislation. Third, the increased knowledge and experience of the cities makes them not only an effective interest group but also makes State regulation less necessary.

The increase in the complexity of cable issues has resulted from the rapid growth and development of the industry, the interrelationships of cable and other communications technologies, and the evolutionary regulatory environment. For example, absent alternative Federal policy, States involved in traditional regulation of the telephone industry will inevitably become involved in deciding "common carrier" issues when cable systems lease channels or provide telephone-type transmission services. Other current issues such as privacy and theft are less complex areas where State legislation can assist both the industry and the public and where State statutes might be beneficial. These issues are not limited to cable but arise also in connection with other technologies with similar capabilities.

Conclusion

State roles during the past twenty years have ranged from laissez faire policies to traditional regulatory approaches. Nonregulatory programs of a developmental or assistance nature have also been implemented in several States, and many deregulatory actions have been taken. At the same time, local control and sophistication in dealing with cable have increased substantially. State roles are likely to continue to vary for the foreseeable future as the issues are further sorted out.

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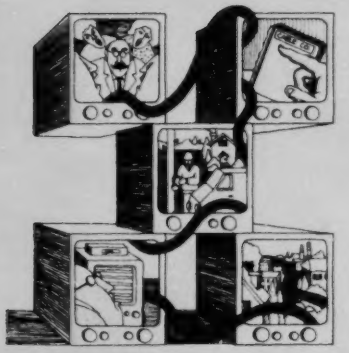

The Franchising Process

*By**
David Owen Korte

*The author and editors gratefully acknowledge the contribution of Philip A. Tymon to this chapter. Some parts of this chapter originally appeared in an article by the author in Public Management magazine, June 1980.

Chapter 3: The Franchising Process

The selection of a cable television company is often one of the most controversial and publicly debated decisions a local government will face. Local elected officials responsible for selecting, franchising, and regulating the cable operator sometimes feel caught between a public that demands cable as soon as possible and the need to proceed slowly and carefully in choosing the best company. The task of franchising need not be overwhelming, however. This chapter describes a general franchising procedure that many large and small cities have used successfully to secure quality cable service for their communities. In essence, a successful process involves careful study, public participation, a realistic timetable, and a procedure that facilitates fair and open competition among all interested cable companies.

The rosy future for the cable industry has sparked tremendous competition for the remaining cable franchises. Such competitive interest means both short-term problems and long-term benefits to cities facing the cable issue for the first time. There is much at stake, and it makes little sense to rush into a decision on awarding a cable franchise no matter how much pressure aggressive cable operators and a demanding public bring to bear.

In past years, it was far too common for an interested cable company to make a pitch to an uninformed city council and, within a few weeks, walk away with an exclusive 20-year franchise. Typically, such franchise ordinances contained little protection for consumers and only vague commitments for cable service. In far too many cases, such systems were never built because the company did not have the necessary financial resources or because it chose to "warehouse" the franchise and use its available funds to build other more lucrative markets. Sometimes the franchise right granted by the city was sold at a healthy profit before construction had begun. In other instances, the system built offered far fewer services than the city had been led to expect.

Even today, some franchises are awarded for basic 12-channel, minimal service systems (with vague promises for more channels in the future when "economically feasible") without competition and without a comprehensive franchise to protect the city in the event the selected operator fails to deliver as promised. If these same cities had taken their time, encouraged competition, and in some cases franchised jointly with neighboring municipalities to offer a large subscriber base, they may well have franchised state-of-the-art systems with substantial commitments for extra services and local programming.

Ideally, a competitive franchising process has three phases: policy development, proposal solicitation, and evaluation/selection. Typically, this process takes nine to twelve months to complete. A longer period is usually unnecessary, but anything less invites mistakes that the community may have to live with for years to come.

The First Phase: Policy Development

The policy development phase is probably the most important in the franchising process. This is the stage for fundamental decisions regarding the franchising process, regulations and minimum service standards. Some major policy considerations include the following:

Form of Ownership

The municipality should decide at the outset whether it wishes to consider some form of public ownership of the cable system, such as municipal or cooperative ownership. (The benefits and risks associated with public ownership are discussed in chapter 6.) The procedure described in this chapter assumes that a private company will be sought.

Many cities are now encouraging minority group ownership and management participation in cable and have established such criteria in their requests for proposals (RFP). Some cities have encouraged local participation in ownership in general, while others have discouraged it, fearing the highly politicized "rent-a-citizen"[1] problem experienced in many recent franchise awards.

Service Areas

Many communities have sectors without sufficient housing density to warrant a requirement that all homes initially be served by cable. In such cases, a minimum primary service area that will be cabled initially should be delineated. Line extension requirements should be established to insure that the system will expand into excluded areas as housing density increases and new territory is annexed. Typically, local governments have required that services always be made available to contiguous areas with a minimum of 40 to 50 homes per street mile.

The local government should also consider defining any districting or multiple franchise district at the outset so that responses from applicants will reflect these service areas. In most instances, however, a single system covering the entire municipality is preferred to insure uniform service and rates.

Local Programming, Access, and Institutional Use Requirements

Many local governments conduct surveys or needs ascertainments to determine the proper level of programming support needed from the cable operator to allow institutions and individuals to use the cable system effectively.

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[1] "Rent-a-citizen" refers to the practice of employing prominent citizens to influence the award of a franchise. Usually a "rent-a-citizen" receives a low-cost or no-cost ownership position in a company if the franchise is won.

Term of the Franchise

Local governments should decide the term of the franchise at the outset. Most franchises are 15 years' duration to allow the operator time to realize a return on investment.

Franchise Fee

The amount of the fee the cable operator will pay the municipality for the right of the franchise should be established by the municipality and not be left as a bid item. Current Federal Communications Commission (FCC) rules limit the amount of the fee to 3 percent of the gross revenues of the system. A higher amount, up to a maximum of 5 percent of gross revenues, is permitted upon a showing to the FCC that the amount is appropriate in light of a "planned local regulatory program." The FCC has held that this amount may include expenditures for regulating costs and the development of local programming.

Rate Regulation

At one time the FCC required all governments to regulate basic subscriber rates. Now, except in the few States that either require local rate regulation or regulate rates on the State level, local governments are free to decide whether to regulate rates for themselves. The FCC continues to prohibit regulation of pay cable rates. It is recommended that local governments at least reserve the right to assert control over rates in the future should market forces fail to keep rates reasonable. (Rate regulation is discussed in detail in chapter 7.)

Regulatory Structure

The governing structure used to regulate the cable operator is also an important policy decision that should be made early. Basic responsibilities include monitoring construction, evaluating rate increase requests, handling consumer complaints, and reviewing company performance. Smaller governments often find that these responsibilities can be handled by an existing staff person. Larger cities may need to hire one or more full-time people. If care has been taken in selecting the operator, however, the ongoing regulatory task need not require an elaborate regulatory structure.

Many cities also assume an ongoing role in promoting and developing public use of the cable system as well as use of the system by the government itself. In such cases, cities may also establish permanent commissions or advisory boards to assume these responsibilities during or after the franchise award. Chapter 10 provides an in-depth discussion of these options.

During the initial policy development phase, local governments usually develop and refine their approach to the rest of the franchising procedure. Often this phase includes beginning a community education campaign (so that citizens understand the complexity of the process); holding public hearings on cable television options; and forming citizen advisory

groups to work with city staff in researching cable television services and technology, conducting community "needs assessments," developing citizen input structures, and making recommendations on items to include in the RFP and ordinances.

Many local governments have found that citizens do not understand the complexity of the franchising process, the amount of time it takes, or even the range of cable television services available. However, this complexity should be no surprise to local officials. Citizens cannot be well informed unless the local government undertakes to inform them, by holding public hearings, insuring adequate coverage of the process in the press, and making special efforts to tell potential users of the cable system about what cable can offer. Many local governments sponsor community workshops and seminars for just this purpose. Local governments can benefit from an informed citizenry in several ways during the franchising process. If citizens are informed, their input and ideas can be valuable during the policy development phase, in drafting the RFP, and in evaluating the applicants' proposals. Moreover, informed citizens are more tolerant than those who do not understand why the city is not taking quick action on awarding a franchise. Finally, many cities are interested in public, educational, and government access channels and facilities. It takes a long time for the public and institutions to gear up to understand and use community programming opportunities over cable. The sooner the community starts to organize to use access, the more likely it is that such programming can be implemented.

In many larger cities, independent citizens' cable coalitions have formed during the franchising process with the intent of influencing policy decisions and the award. Unless these groups are brought into the process early and integrated into the city's information gathering efforts, animosity may develop between the citizens' groups and the city staff or decision-makers.

The policy development phase concludes with the drafting of one or more ordinances and the RFP. As discussed in chapter 4, the ordinances detail the policy decisions and regulatory requirements of the local government. Drafting the ordinances at this phase and including them with the RFP insures that all prospective applicants understand the city's regulatory decisions before submitting an application. This approach greatly simplifies final negotiation of the franchise agreement with the selected company.

The RFP should give the deadline for submitting applications and describe all minimum requirements and desired services. The government's evaluation criteria are sometimes also included. The RFP should specify clearly the form and content required of any application submitted. Including such information is particularly important. Understandably, applicants tend to be as vague as possible in order to give themselves more latitude in operating the system in the future. But it is in the local government's best interests to require that applicants be very detailed about their proposed systems and services to provide a complete basis for comparing and evaluating the proposals. A detailed proposal also helps the local

government compare the future performance of the selected company against its initial promises.

To achieve uniform content and structure of each application, the local government should supply an extensive set of forms to be used by each applicant. At a minimum, the following information should be solicited:

- Full ownership disclosure of the local company and parent company (if any);
- Verification of adequate funds;
- Detailed financial pro forma projections for the system;
- Technical design, layout, and channel capacity;
- Construction and maintenance practices;
- Technical performance standards;
- Programming to be provided, including broadcast TV satellite programming, automated programming, and text and local origination programming;
- Access channels, production facilities, budgets, and staff;
- Proposed rates for all services; and
- A list of the applicant's other cable systems, any systems owned in the past, and a list of other applications pending.

For all but the smallest cities, it is reasonable to expect that all of the city's franchising costs will be recovered from the applicants. A nonrefundable application fee is usually specified in the RFP—typically $500 to $5,000 depending on the size of the city. Some major cities have required as much as $10,000. Further, the RFP should provide that the selected company will reimburse to the city all additional franchising costs not covered by the application fee up to a reasonable limit. Current FCC rules provide that any initial payments to a local government in excess of the government's actual franchising costs may be credited by the company against future franchise payments due.

Often, local officials are confused about the extent to which services must be required. For instance, institutional networks most often are not required. Access requirements are usually minimal: one channel for public access, one for educational access, one for municipal access, and one for leased access. Two-way capacity usually is not required in the RFP. The strategy of most cities has been to keep requirements to a bare minimum. Since the competitive application process will, in many areas, solicit the best service packages and rates for a cable market, there is no need to require more than minimum standards. Still, however, applicants need guidance in preparing their bids. Thus, cities often clearly state preferred levels of service and give an idea of their decisionmaking criteria in the RFP. Too many requirements may leave a city with no applicants for the franchise, so, wherever possible many cities have kept requirements minimal with excellent results.

The Second Phase: Proposal Solicitation

After the RFP is approved and published, a notice of its availability usually appears in a local newspaper and at least one national trade publication. Companies usually have at least three months to prepare and submit applications.

Often by the time the RFP is drafted, and sometimes long before, several cable companies are already present in the community. In large cities an applicant may set up a local office and hire a local franchising staff long before the RFP is released. Local owners, usually with political connections, are recruited in the community. Applicants survey local institutions, municipal agencies, and community groups for their "needs" for access and other cable services. Each competitor is vying for a local identity that will help to win the franchise. Often, however, their public relations efforts can disrupt city agency staff and other institutions. In most cases, the cable companies are collecting necessary and useful information, but some applicants may begin to exert political pressure on local decisionmakers to insure a favorable award. Thus, many local governments have passed ex parte or no-contact rules to insure that no improper contact takes place between applicants and local decisionmakers.

The Third Phase: Evaluation and Selection

Today it is not uncommon for a municipality to receive four to ten franchise applications, and in many cases the quality of each application is high. Generally, for any given city more than one franchise applicant could provide adequate or superior service. Franchise applications have become voluminous, highly technical, and complicated to read. One recent applicant's proposal in a major city consisted of eight volumes of information. In reviewing and evaluating the responses to the RFP, technical assistance can be very helpful.

Each application should be reviewed first for internal consistency and for the feasibility of the proposed plans. Applicants should have clearly demonstrated the financial resources necessary to build the proposed system and to operate it until it becomes profitable, often as long as five years after startup. Projected capital expenses, revenues, and rates should be realistic and insure good performance and a reasonable but not excessive return to the system owner. The technical design must be sufficient to permit the delivery of all the services proposed initially, as well as provide the flexibility and surplus capacity to permit adding programming and services as they become feasible in the future. Responses to all forms should be cross-checked for consistency; for instance, noting whether the access personnel listed in the services section were budgeted in the financial section. More often than not, the evaluators will find that the proposals contain several inconsistencies and vague or contradictory language. Thus, local governments may want to allow time for clarification of bids before final evaluation or ranking of the proposals is made. At this point, however, most local

governments will not allow bid improvements to be made. After the applicants have seen each others' proposals, they may be tempted to use the clarification period to upgrade certain aspects of their bids. Local governments that allow bid improvements, however, may risk legal challenges from the other applicants.

A side-by-side comparison of the financial, technical, and service aspects of the proposals should then be made. A well-structured RFP will make this task considerably easier. Vague promises for services qualified by words such as, "when there is sufficient public demand," "may," or "when economically feasible" should be ignored. Such promises are difficult if not impossible to enforce, and a particular applicant should not be favored simply because it offers the longest laundry list of "possible" future services that all applicants could provide.

Decisionmakers should also evaluate the performance records of the applicants in serving other communities. Some applicants will offer to fund field trips to one or more of their existing systems. These trips are usually of little value, however; most cable operators have one or more "flagship" systems that they want to show off. An applicant's overall track record is more important than a particularly good performance in a few cities. The best approach is to contact directly city officials in communities now served or served in the past to ask whether the company lived up to promises made, whether subscribers have complained excessively, and whether the company resolved complaints fairly and expeditiously. Also, city officials will want to know how cooperative the company has been in working with local officials to resolve problems. This type of information will give a much better sense of how a particular company will perform than a field visit to one of its systems.

Before a final decision is made, at least one public hearing should be held to present the findings of the evaluation report and to hear final presentations and clarifications from the applicants. Citizens should also be given the opportunity to comment on the applicants and their proposals. In recent years, company presentations at such hearings have evolved into elaborate multimedia shows, often with extensive equipment displays. The hearing should be well structured, and applicants should be given time limits on their presentations.

Even after careful planning and evaluation, the final choice may not be an easy one. In recent years, competition among cable companies has often placed local governments in the enviable but difficult position of having to choose among two or more excellent proposals. A decision must rest not only on which applicant offers the "most" or the "best" but also on more subjective but nevertheless important considerations such as "Which firm has been the most responsive to this community?" and "Which has the track record, experience, and commitment to deliver on all promises made?"

An experienced consultant can provide valuable assistance to a local government in the franchising process by supplying information, conduct-

ing workshops, identifying key issues, drafting ordinances and the RFP, and helping in the difficult task of evaluating the proposals. It is important that a consultant, if used, should be brought in at the start of the process.

Municipalities should select cable consultants carefully. A consultant should have a proven track record in providing assistance to other local governments. Some cable consultants also work for cable companies. Any potential conflict of interest should be investigated because a consultant under consideration may have also worked for a potential applicant. A good consultant can save wasted time and help the city learn from and avoid mistakes made by other cities.

Several local governments have experienced litigation as a result of their franchise decisionmaking process. Pittsburgh, Houston, and Minneapolis have been involved in lawsuits that involved the cable franchise award. Some have jokingly called franchise litigation "the appeals process," but to local governments there is nothing funny about being sued. No award method is guaranteed to avoid a lawsuit, however. The value of the franchise is often high enough that losing applicants might feel they can afford to take one more shot at it by attempting to invalidate the award and open the process up for bidding again. The best approach a city can take is to insure that the process has been fair and open, that the established procedures have been followed, that the evaluation was accurate and fair, and that no improper political influence was allowed to affect the decision-making process.

Joint Franchising

Many smaller cities have found it beneficial to join with contiguous local governments in the franchising process. This approach may afford smaller communities several benefits. First, by joining together, either through a joint powers arrangement or by agreeing to issue a common RFP, the total area may have a large enough subscriber base to allow more attractive proposals for sophisticated and extensive services. Second, often such areas share other municipal services, such as school districts or service agencies, that would benefit from being on the same or an interconnected cable system. The joint franchising or joint award to one company would allow such interconnection automatically. Third, a joint franchise agreement can be designed to insure that rates for equivalent services will be consistent among adjoining communities and that future rate increase requests can be negotiated collectively. Joint franchising, however, is successful only if all participating jurisdictions agree from the beginning to reach a common decision. A split decision on the award may mean that none of the participating jurisdictions will benefit from the economies of scale reflected in the proposals.

Summary

The franchising process can be long and complex, but municipalities

must remember that the decision to award franchise to one company is binding for a decade or more. The cable communications system in a community can be a vast resource of new revenue for the city, and new jobs, and new services. Moreover, citizens will demand the best cable service possible. Thus it makes sense for local governments to proceed slowly, cautiously, and methodically toward a franchise award.

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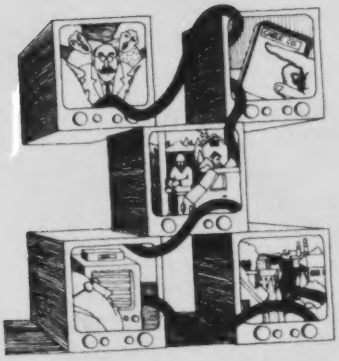

The Cable Television Ordinance

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*The authors and editors gratefully acknowledge the contribution of Philip A. Tymon to this chapter.

Chapter 4: The Cable Television Ordinance

Because a cable television system depends on cable lines and other equipment being strung on poles over or buried under city streets, a cable company must obtain municipal permission to use public rights-of-way. Two documents are normally involved in granting this permission—the ordinance and the franchise. The cable television ordinance is the basic regulatory document governing cable operations and administration in the city. The franchise is the permit or license to operate that a specific cable company receives from the city. The franchise is usually contractual in nature because it is signed by both the city and the company.

The terms ordinance and franchise are often used interchangeably, sometimes mistakenly and sometimes correctly, because the ordinance and franchise agreement can be combined into one document called the franchise ordinance. In contrast to the franchise ordinance, which conveys the right to do business to a designated cable company, the regulatory ordinance contains provisions that enable the granting of a cable television franchise and states the rules and regulations with which any cable television operator in the city must comply. A city with a regulatory ordinance enters into a separate franchise agreement with each cable company. A regulatory ordinance can be amended unilaterally by a city council. Such an amendment becomes problematic only if it materially affects the terms of the franchise agreement. The franchise ordinance, on the other hand, may be more difficult to amend without the consent of both parties.

The city's power to enact such ordinances is most broadly based on its general police power. In many States, however, stronger authority is provided by specific State statutes or is contained within city charter provisions. The specific source of authority varies widely from State to State and among the subdivisions within a State.

A local government has unilateral authority to supervise the safe use of its streets and rights-of-way and to protect the safety of its citizens. The scope of this authority is uncertain as a local government extends such regulation to other elements of the cable system not directly related to public safety, and the use of its streets, such as rate regulation, service requirements, and other extended regulatory concerns. To the extent the city enjoys delegated powers from the State to regulate economic activity, whether explicit or implicit, the city can use this further authority to regulate cable services. And to the extent the cable franchise ordinance is a voluntary contract accepted by the cable company, the company is bound by the contract's terms, whether or not the city had legal authority to impose unilaterally the same regulatory conditions.

The provisions of a cable television ordinance usually fall into three categories: general provisions that include the rights of the company to do business, specific provisions that include the city's minimum requirements for operating the system, and administrative and regulatory provisions that include penalties for noncompliance.

Although cable ordinances adopted by local governments in the past may have contained these categories, their primary focus was the granting of business rights to the company. Today, enacted ordinances incorporate specific provisions for administration and regulation as well as specific technical, service, and operational requirements. These provisions are designed to insure that the cable operator's performance conforms to its initial promises. A brief discussion of key provisions in the three categories follows.

General Provisions

This category includes clear definitions of important words found in the ordinance. It also includes a statement of the purpose of the ordinance and of the city's authority to grant and to regulate. (In a regulatory ordinance, provisions establishing the procedures by which the city will grant franchises are included in this category. In a franchise ordinance, provisions granting a franchise to a designated cable company and incorporating by reference that company's franchise application are included in this category.) The rights granted to a franchisee, such as length of franchise, are listed. The responsibilities of the franchisee to guarantee performance, such as providing construction bonds, insurance, and indemnification, are explicitly stated. Some key general provisions include the following:

Grant of Right of Franchise

This provision grants the rights to a particular company to build and operate a cable system and to sell cable services subject to the terms and conditions of the ordinance as well as applicable local, State, and Federal laws and regulations. Although it is usually preferable to award a franchise to only one entity for a given geographic area, most franchises are nevertheless granted on a nonexclusive basis.

Franchise Term

Most local governments grant a franchise for a 15-year term. A shorter term makes it difficult for the company to earn a reasonable return on its investment and may even discourage applicants from applying for the franchise. A short term may also result in higher rates or less comprehensive services.

Incorporation of Proposal

In almost all cases, the selected applicant has proposed substantially more than the minimum requirements and standards of the local government. The ordinance should incorporate the company's entire proposal as well as any additional clarifications or offerings made by the company's representatives during the franchising process. This provision should also provide that in the event of conflict between the proposal and the ordinance, the provision that provides the greatest benefit to the local government, in the opinion of the local government, shall prevail.

Franchise Territory

The ordinance should specify the exact area covered by the franchise. In most cases, the franchise is for the entire geographic area of the municipality as it exists and as it may change during the franchise term.

Franchise Fee

Most local governments require a franchise fee, usually based on a percentage of the gross revenues of the company's operations within the franchise area. Current Federal Communication Commission (FCC) rules limit the amount of the fee to 3 percent of gross revenues. A higher amount, up to a maximum of 5 percent of gross revenues, is permitted upon a showing to the FCC that the amount is appropriate in light of a "planned local regulatory program." The FCC has held that this amount may include expenditures for regulating costs and the development of local programming.

The provision should specify the amount of the fee and the frequency of payment—usually within 45 days of each quarter of the company's year. The company should also be required to file verified statements showing how the amount of fee was calculated, and the local government should reserve the right to inspect and audit the company's financial records if it has any doubt whether full payment was made. Many local governments also specify an interest penalty for late payments.

Police Powers

This provision provides that the rights granted to the company are subject to the police powers of the local government to adopt and enforce general provisions necessary to the safety and welfare of the public.

Construction Bond

A bond should be required to help guarantee the timely construction and full activation of the system. The amount of the construction bond varies but is usually 10 to 20 percent of the estimated construction costs of the system. The bond may be terminated only after the local government determines that the initial construction has been completed in accordance with the terms of the ordinance.

Some local governments also require a performance bond to be maintained throughout the franchise term. Because of the difficulties in using a bond as an enforcement tool for minor breaches of an ordinance, however, few governments have sought to make a claim for payment of the bond for any purpose other than for failure to construct the system. Other remedies, especially the establishment of a security fund, have proven far more workable and effective.

Security Fund

This provision requires the company to maintain an ongoing cash fund or letter of credit, usually $10,000 to $50,000, from which the local

government may withdraw unpaid franchise fees, taxes, and penalties for violations of the ordinance. The provision requires that upon a withdrawal by the municipality, the company must restore the fund or credit to the full amount. If a cash fund is required, the company is usually permitted to receive any interest earned. A security fund is a much easier enforcement tool for the government than a performance bond and also is less expensive for the cable operator.

Indemnity and Insurance

This provision provides that the company will hold harmless and defend the local government from any charges or claims resulting from any action by the company or the government itself arising out of or connected with the installation and operation of the cable television system. It should also specify the minimum amounts of liability insurance to be maintained by the cable company.

Rights of Individuals

With the addition of new services requiring the transmission of information from as well as to private homes, individual privacy is of growing concern. The ordinance should prohibit the company from installing any service that involves the transmission of any signal from a subscriber's home or business without the subscriber's written permission, which may be revoked at any time without penalty. Likewise, the company and the local government should be prohibited from selling or otherwise distributing lists of the identity or viewing habits of any subscriber without written authorization.

The company should also be prohibited from denying service, access to the system, or employment or otherwise discriminate against subscribers, channel users, or general citizens for any reason.

Specific Provisions

This category includes specific requirements for the construction and operation of the cable system. It also includes required technical and service standards. The regulatory ordinance sets, under this category, minimum requirements that a franchisee must meet. Because these minimum requirements are not only met but often exceeded in the franchise application, the franchise ordinance substitutes what the applicant has specifically proposed for the general minimum requirements. Some key general provisions are as follows:

Cable System Construction

This provision describes the minimum amount of construction and activation of the system to be accomplished each year either as a percentage of the total amount or, if possible, by defined areas. Most cities have sufficient housing density to justify a requirement that upon completion, service

must be available to all dwelling units. Some local governments containing areas of low housing density initially may need to exclude such areas from the service area. However, any area that will not be included in the initial service should be carefully defined in the ordinance. Most often this is accomplished by specifying that service must be extended to all contiguous areas having a density of at least 30 to 50 dwelling units per street mile.

It is also advisable to include a "line extension" requirement that service must be extended to households in areas that do not satisfy the established minimum density upon payment by the subscriber of the incremental cost of the extension. This insures that any household can receive cable service but that service to subscribers electing to live in low-density areas is not being unreasonably subsidized by the other system subscribers.

Services

In addition to incorporating the company's entire franchise proposal, by reference it is advisable to list in the ordinance the specific services the company will be providing. Any ambiguous offerings in the proposal should also be clarified in the ordinance.

Access

The provision of public, educational, government, and leased access channels on a first-come, nondiscriminatory basis is no longer required by the FCC. This leaves each local government with the responsibility for establishing the right of access to the cable system. The company's franchise proposal, which should be incorporated into the ordinance by reference, usually describes (a) the number of channels to be reserved; (b) the amount of staff and production equipment the company will provide to support the development of access programming; (c) rates, if any, for use of the channels and equipment; and (d) the company's policies on promoting and administrating access. The ordinance nevertheless should contain specific provisions requiring the company to provide nondiscriminatory access to the system.

Underground Construction

The cable company should be required to place its cable underground in areas where both power and telephone utility lines are underground. This provision insures that no new poles are installed.

System Interconnection

The company should be required to cooperate and share reasonably in the costs of interconnecting at least local programming channels with any other cable system upon direction from the local government or other State or Federal agency established for the purpose of interconnecting cable systems.

Construction, Maintenance, and Technical Standards

The ordinance should specifically require compliance with appropriate local and national construction, maintenance, and performance standards. It should also incorporate by reference any such standards proposed by the company in its application. Other items to be addressed in this provision include the maintenance and availability to the local government of construction maps, records, and technical data; minimum interference with persons and existing buildings and public ways; restoration of damaged property; relocation of facilities as requested by the local government; minimum interference with utilities; and tree trimming.

Continuity of Service Mandatory

The company should be obligated to provide continuous, uninterrupted service to its subscribers during the term of the franchise even if the local government gives notice of its intent to terminate or not renew the franchise. In the event the company fails to provide service for a specified period, usually three to seven days, the local government should reserve the right to operate the system until the company restores service under conditions acceptable to the government or until a new operator is selected.

Transfer of Ownership or Control

The ordinance should prohibit the transfer of ownership of the company or any change in the actual working control of the company without the prior consent of the local government.

Availability of Books and Records

The company should be required to cooperate fully and make available for inspection by the local government all books, records, maps, plans, and other like materials of the company upon reasonable notice and during normal business hours.

Complaint Procedures

The company should be required to keep a local office open during normal business hours for the purpose of receiving and resolving complaints regarding the quality of service. The company should also maintain a local, toll-free telephone number and be able to receive complaint calls 24 hours a day, seven days a week. The ordinance should specify the maximum time for acting upon and resolving complaints. The company should also keep a maintenance service log indicating the nature of each complaint, when it was received, and how and when it was resolved. This log should be maintained for at least two years and be available for inspection by the local government.

The ordinance should require the company to provide each new customer with information on how to make inquiries or complaints and the appropriate government office to contact if the company fails to resolve the subscriber's complaint.

Removal of the System

Upon expiration or termination of the franchise, the local government should reserve the option to require the company to remove its facilities from all streets, public ways, and public places and to restore any public or private property to its condition prior to the installation of the system at the company's own expense. Some governments have required the posting of a bond to cover the cost of system removal.

Administrative and Regulatory Provisions

This category includes specific rules and procedures to help the city enforce compliance by the cable operator with the terms of the franchise. Technical and financial reports are required from the cable operator; procedures for setting and changing rates are specified. Methods for periodic system performance review and evaluation and penalties for noncompliance are established. Some key provisions are as follows:

Amendment Procedures

Specific procedures for processing requests by the company to amend the ordinance should be described fully.

Rates and Rate Setting

The FCC no longer requires local governments to regulate the rates of the cable company. Therefore, except in the few States that either regulate rates on the State level or require local rate review, local government regulation of subscriber rates is optional. Current FCC rules prohibit any regulation of pay cable rates.

At minimum, the ordinance should reserve the right to assert jurisdiction over rates in the future. Most local governments, however, elect to regulate rates from the outset. In such cases, the initial rates for services should be listed in the ordinance or as a separate agreement with the company. It is common to specify that no adjustment of rates will be considered until after initial construction of the system is completed.

Generally, the procedures for processing a rate increase request are the same as apply for any ordinance amendment. The ordinance also should be specific about the financial information the company should supply to support its rate increase request.

The ordinance should also describe the factors the government will consider in evaluating the request, including maintenance of a fair rate of return to the company, management efficiency, compliance with the terms of the ordinance, the quality of service to subscribers and users, and the company's willingness to upgrade the system and services.

Performance and Evaluation Sessions

Many ordinances contain schedules for public evaluation sessions, usually held every three to five years, at which the performance of the com-

pany is reviewed. Such sessions may also be held at any time upon a finding of need.

Governance

At minimum, the ordinance should identify a particular staff person to be responsible for the continued administration of the franchise. Some local governments have established a separate agency, commission, or advisory committee to regulate cable television. (See chapter 8 for a discussion of these options.)

Penalties or Liquidated Damages

The ordinance should specify penalties (often expressed as liquidated damages) for violations of the ordinance. Usually expressed in terms of "x" dollars per day, such penalties are chargeable to the security fund discussed previously. Such penalties typically cover failure to meet the construction deadlines; failure to provide data, documents, reports, or information as required or upon request; failure to meet construction, maintenance, or technical standards; the sale or distribution of information about subscribers without written authorization; and failure to comply with any other requirement of the ordinance or applicable law.

Forfeiture and Termination

The ordinance should clearly provide the right of the local government to terminate the franchise in the event of a substantial breach of the terms and conditions of the ordinance.

Foreclosure

In the event of foreclosures or other judicial sale of the system, the ordinance should provide that the provisions covering transfers of ownership or control shall apply.

Receivership

Within a reasonable period following the appointment of a receiver or trustee for any reason, the local government should reserve the right to terminate the franchise.

Renewal

The ordinance should specify the procedures for reviewing a renewal request by the company. The process should begin at least one year and preferably two years before the expiration date of the franchise in order to provide adequate time for public review of the performance of the company and, should negotiations not yield satisfactory results, to solicit applications from other companies. The existing company should be given a reasonable opportunity to justify a renewal, but the ordinance should not include any language that would confer an option to renew in favor of the company that would limit the local government's right to seek other applicants.

Other Optional Provisions

Although less commonly used, the following provisions should be considered for inclusion in a franchise or regulatory ordinance.

Purchase by the Local Government

Many local governments include in their ordinances the option to purchase the system upon expiration or termination of the franchise. Usually, the purchase price of the system upon expiration is based on the "fair market value" of the system less the value of the franchise right. In the case of termination of the franchise for cause, many local governments use "book value" as a basis for determining the purchase price. It should be assumed that, regardless of the basis used, agreement between the local government and the cable company on the purchase price will not be reached easily. Therefore, it is advisable to include a binding arbitration clause in the ordinance.

Assertion of Local Regulatory Authority

Federal courts, the FCC, and Congress are constantly considering challenges to specific local, State, and Federal regulations of the cable industry. The FCC has gone from light to heavy and back to light regulation of the cable industry. Local governments should not assume that the regulations in place at the time of franchising will remain the same over the 15-year term of a cable franchise. To protect against this uncertainty, many municipalities include in their ordinances language to allow adoption of additional local regulation when and if permitted by State and Federal authorities.

Theft of Service and Tampering

The problems of malicious damage to the cable system and the taking of cable services without payment should be of concern to subscribers and local governments as well as cable companies. A few States have adopted theft-of-service laws covering cable service. In the absence of appropriate State or local statutes, a local government should include such a provision in its cable ordinance.

Censorship

The objective of free speech by means of cable television is sometimes countered by the concern for the presentation of certain programming deemed by some to be objectionable—including, but not limited to, obscene or indecent material. The issue of whether certain programs should be prohibited from carriage is a controversial one that is best determined by each community.

Many local cable ordinances have delegated sole responsibility for the content of programming to the cable operator. Yet, some channels—especially those reserved for public, educational, government, or leased

access purposes—carry programming that is or should be beyond the control of the cable operator.

It is suggested that the ordinance place responsibility on the program producer for the content of any particular program on an access channel. The particular programmer in each case should be solely accountable for violations of any applicable laws concerning obscenity, libel, or slander. Likewise, the ordinance should prohibit both the cable operator and the local government from censoring or otherwise exercising prior restraint over the content of non-operator-produced programming.

Landlord/Tenant Relationship

A serious problem for cable companies and potential subscribers has resulted when owners of apartment buildings prohibit cable service from being provided within their buildings or demand excessive payments from the company for the right to serve tenants. Unless covered by appropriate State law, ordinances should include a provision prohibiting landlords from interfering with the right of tenants to receive cable service. The landlord would be permitted to establish reasonable conditions on the cable operator necessary only to protect safety, functioning, appearance, and value of the premises. Compensation to the building owner for the right of access, if any, would be limited to a nominal sum.

Summary

Setting forth the rights and responsibilities of both the cable operator and the local government, the cable television ordinance is the "rulebook" for the cable regulation at a local level. The importance of a comprehensive, precisely worded ordinance cannot be overstated. Ordinances that do not detail specific provisions for administration and regulation as well as operational, technical, and service standards and requirements cannot insure that the franchisee will perform as promised. Similarly, provisions written in ambiguous language may lead to disputes between the city and the cable system operator. Thus, the more specific the provisions of an ordinance, the more effective a tool it is for enforcing compliance.

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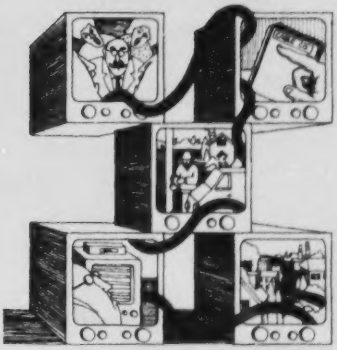

Overbuilds And Districting

By

John Mansell

Chapter 5: Overbuilds and Districting

A crucial issue for local government decisionmakers is choosing which, and how many, cable operators should provide service in an area. The traditional model, used in the vast majority of cases, is to assign a given area to a single private cable company. But several cities have franchised competing companies to operate cable service in the same area. When two cable companies compete "head-to-head" for subscribers, the situation is called an "overbuild."

It is becoming increasingly possible that cable companies will seek permission to "overbuild" existing franchises. Some may seek a second franchise in order to take over the existing company or put it out of business. Others may simply desire to compete. In the past, both economic disincentives and an unspoken agreement among cable companies have discouraged "claim jumping" of existing franchisees. This industry attitude is likely to change because of new economic considerations and the *City of Boulder* decision, which increases the likelihood that municipalities will grant multiple franchises.

To date, fewer than two dozen local franchising authorities have licensed competitive cable operations to "overbuild" each other in the same territory. A state-of-the-art cable system in a major city can be expected to cost $15,000 to $20,000 per mile to construct. Assuming a potential of 100 homes to the mile and a penetration rate of 50 percent, this investment should yield 50 subscribers per mile at a cost of about $350 each. If two companies share the same franchise area and are equally matched in talent and resources, it stands to reason that they would likely split the market in half. With each obtaining only 25 subscribers per mile, they would thus double their effective investment per subscriber. Such a prospect would not be viewed favorably by the lending institutions that finance cable development or by the company's shareholders. The limited history of overbuilds is filled with stories of higher costs—the result of expensive sales promotions and attendant legal and engineering expenses—and of mergers and sellouts.

The following list notes cities that had two cable systems where one company either went out of business, merged with a competitor, or reached an accommodation with the city:

Austin, Tex.
Brookhaven, N.Y.
Burlington, Wash.
Charlotte, N.C.
Columbus, Ohio
Corning, N.Y.
Dansville, N.Y.
Frankfort, Ky.
Jefferson Parrish, La.
Longview, Wash.
Manatee, Fla.
Owenboro, Ky.
Pensacola, Fla.
Pottsville, Pa.
Salisbury, Md.
Tallahassee, Fla.
Warrenburg, Mo.
Williamsport, Pa.

Currently the following communities have licensed overbuilds:

Allentown, Pa.	Huntington, N.Y.
Bryan, Tex.	Muscle Shoals, Ala.
Chester, N.Y.	Paramus, N.J.
Dade County, Fla.	Phoenix, Ariz.
Hartselle, Ala.	Presque Isle, Maine
Hillsborough County, Fla.	Slidell, La.
Hillsdale, N.J.	

Allentown, Pennsylvania, is the single case so far of a "successful" overbuild in which two companies have built their systems on the same streets. This situation has resulted in both companies offering essentially the same service for the same price and, arguably, it has drained each of the resources that might otherwise be available for additional subscriber services, as shown below:

Category	Service Electric	Twin County Trans-Video
Channel capacity	30	27
Homes passed	80,000	82,500
Basic subscribers	34,000	57,000
Basic monthly rate	$7.50	$7.65
HBO subscribers	6,000	5,842
HBO monthly rate	$8.95	$8.00
Prism subscribers	2,250	2,542
Prism monthly rate	$8.00	$9.00
HTN subscribers	1,000	n.a.
HTN monthly rate	$9.50	n.a.
Movie channel subscribers	n.a.	2,500
Movie channel monthly rate	n.a.	10,000

It is questionable whether overlapping franchises improve the variety of service offerings or the speed of expanded service introductions. Indeed, multiple franchising may retard construction because delays may occur in obtaining the pole attachment rights. Consider Phoenix, Arizona: American Cable TV was awarded a 15-year franchise in 1976, with construction required to begin by the end of 1980. In September 1980, when less than 10 percent of the system had been completed, the Phoenix City Council decided to award new citywide licenses to two other companies and a permit for a limited 128-mile area to a third firm. The two citywide licenses required the firms initially to build areas bordering their respective starting points. When those areas are completed, the companies may apply for permits to serve areas already cabled. Because of litigation over which firm gets the first pole attachment clearance by the end of 1981, the two 1980 citywide licensees had completed fewer than 100 miles, only about 4.5 percent of the

system. Additionally, in 1982, one of the new Phoenix licensees sold its interest out to the other, without completing construction.

Similarly, the award to two franchisees in Paramus, New Jersey, according to a 1980 report by the New Jersey Office of Cable TV, resulted in higher construction costs, slower construction, and public safety problems. If Paramus had been a single franchise town, said the report, Paramus residents could have received service in half the time. The New Jersey report said cut-throat competition in the early phases of construction led to hazardous traffic safety conditions and damage to telephone facilities. New Jersey Bell Telephone claimed that numerous telephone drops were cut or damaged and that "flipping" cable TV wires into power lines resulted in electric burns on telephone cable that could have caused serious injury or death to cable or telephone technicians.

Communities such as New York City, Seattle, and Dade County, Florida, have had success with "districting"—awarding several cable companies citywide franchises at the same time but requiring each one to begin construction at a different geographic starting point. Once a company completes its district, it may apply for a permit to wire areas that others have already cabled. In most cases, however, cable companies have not expanded into cabled districts because of the high costs and reduced subscriber potential. If a city draws districts that are too small or awards too many franchises, it risks sacrificing the long-range benefits of economies of scale and competitive bidding (for example, higher channel capacity, lower rates, and more services).

Whether or not a cable system is profitable is a matter of public interest because economic injury to an existing system would affect the quality of service.

Still another problem with overbuilds is signal leakage. If signal leakage exists, interference may be visible on the TV screen. This problem can be minimized by constructing systems with well-insulated cable and amplifiers and by separating the cables. Nevertheless, both systems must be installed and maintained according to extremely high standards. The margin of error in such a situation is narrow. If one of the two cable networks is not properly constructed, it could distort the signal of the other system. Another problem can occur when more than two or three cable networks are permitted to clutter city streets with unsightly wires. Recently, the Tenth Circuit Court of Appeals in *Community Communications Co. v. City of Boulder,* 660 F.2d 1370 (10th Cir. 1981) said cable operators are entitled to First Amendment protection, but that this protection is limited because they must disrupt the public domain to disseminate information:

> . . . (a) cable operator must lay the means of his medium underground or string it across poles in order to deliver his message. Obviously, this manner of using the public domain entails significant disruption, especially to streets, alleys, and other public ways. Some form of permission from the government must, by necessity, precede such disruptive use of the public domain. . . . A

> city needs control over the number of times its citizens must bear the inconvenience of having its streets dug up and the best times for it to occur. Slip. op. at 17.

In addition to the question of access to poles, there is the issue of access to multiple-unit dwellings in overbuild situations. Usually an apartment building owner will allow only one company to wire the building. In Brookhaven, New York, for example, during the period when there were two competing companies, access rights were usually granted to the highest bidder. As a result, one of the primary justifications for granting more than one franchise—greater choice for consumers—was more apparent than real because landlords, not consumers, decided who would wire a community.

For all these reasons, a city is wise to conduct a thorough study of cable TV before deciding to award more than one franchise. In addition to mergers, construction delays, access to easements, and regulatory problems, overbuilds often lead to protracted litigation that may involve the franchising authority. Most cable franchises are nonexclusive, but this does not mean that franchising authorities are obligated to issue additional franchises to other parties who subsequently request franchises. Rather, it simply means that the community retains the option to grant additional franchises if the original franchisee fails to live up to his obligations. Absent a showing of such a failure by the original franchisee, the community must carefully consider the long-range realities of overbuilds.

So long as a large number of cities are without cable service, competition among companies seeking new franchises will be focused on these communities. Within one or two years, however, most of the more desirable areas will have awarded franchises, and the available markets will become more limited for those companies pursuing continued growth. Because the cost of acquiring existing systems continues to skyrocket, the economic disincentives to overbuild certain markets may be reduced. This situation exists particularly in highly penetrated markets (70 percent or higher subscribership). Furthermore, large, multiple-system operators may be willing to undercut the rates of competitors and wait out negative cash flows until they can dominate the market. As a result, more and more municipalities will be faced with applications for additional franchises in areas already cabled.

Rejection of an application for a second franchise is the kind of action that may lead to antitrust problems. As discussed in chapter 12, the antitrust laws do not compel cities to grant all franchise applications. Rather, the test is the reasonableness of the decision and the overall effect on competition. It will take years of litigation to establish guidelines on municipal actions in this area. In the meantime, decisions should be made with the advice of antitrust counsel and on the basis of a careful examination of the benefits and the drawbacks of overbuilds.

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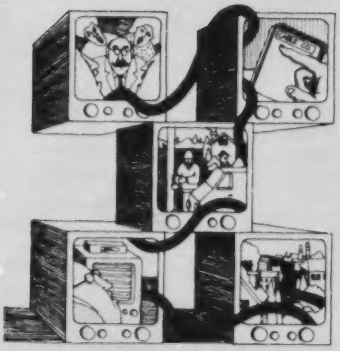

Public Ownership Models

*By**
Jean Rice

*The editors gratefully acknowledge the contribution of John Mansell on this subject.

Editor's Note

Municipal ownership of cable has become a hotly contested issue in recent years. The growing interest in municipal control of cable systems has prompted an energetic response from private cable operators who wish to preclude the municipal ownership option through prohibitive legislation.

Most of the pros and cons concerning public ownership of cable are discussed in the following chapter. The editors wish to add one more point to the debate, however, concerning the potential conflict of the regulator also being the "regulatee." Local governments pursuing a joint venture, or full government ownership may find themselves in an awkward regulatory role concerning both program content and ratemaking; when their goal to profit from the system conflicts with their regulatory role to "watchdog" its services and rates. This problem can be minimized by insulating the programming function from local government through a separate programming authority. However, program decisions are inexorably intertwined with revenues, and the total viability of the system. The responsibility then, ultimately rests with the owner. A municipality with a public responsibility to recoup system expenses may face the need to control programming in order to control revenues and expenses.

Chapter 6: Public Ownership of Cable

Public ownership of cable television systems has become an increasingly attractive consideration to local officials in recent years. The deregulatory mood of Congress and the FCC, the enhanced capacity of cable to deliver public services, and the potential revenues from publicly owned systems have fueled local government interest in exploring alternatives to private, commercial ownership of cable.

Though publicly owned systems are a small segment of the total cable industry, they have had a long, successful history. The first publicly owned systems began operation in the early 1950's, and currently there are more than 30 municipally owned systems and over 30 cooperative systems in operation. Several more cities are actively pursuing alternative ownership options. The most common approaches to public ownership have been municipal and cooperative (subscriber owned) ownership, although local governments have also pursued various forms of joint venture agreements with private companies.

Municipal Ownership

There are several organizational models for municipal ownership: use of an existing agency (for example, an electric or water utility); creation of a new, city department or free-standing city authority; and creation of an independent, nonprofit corporation.

In municipalities where the city already owns electrical or water utilities and operates them through a city department or an independent authority, cable usually follows the same ownership and administrative pattern. This is the case in Wyandotte, Michigan, where city-owned utilities are operated by a city department that has also been given the responsibility of cable television.

Frankfort, Kentucky, owns one of the oldest municipally owned cable systems in the country. This cable system is operated by an independent, nonstock corporation, the Community Service Corporation (CSC). The CSC has a six member board of directors serving staggered terms, named by the Frankfort Electric and Water Plant Board. The board owns the system, provided the original capital for construction, and has a ten-year contract for provision of cable service with the CSC.

Another approach is the nonprofit corporation. This model, which has been considered in St. Paul, Minnesota, and other cities, helps insulate system operation from political control and allows the nonprofit corporation to seek funds from sources the city cannot tap.

Any consideration of municipal ownership or other public ownership models requires an analysis of applicable State laws, since each State gives municipalities different powers. For example, Alabama and New York give cities explicit authority to own their own systems. Some States re-

quire approval by public referendum and others have no explicit legislation.

Financing for municipally operated systems can come from several sources. Cities that operate utilities usually borrow from them. The city of San Bruno, California, for example, borrowed $500,000 from its municipally owned water department. The city of St. Paul, Minnesota, has considered financing a nonprofit cable corporation by having its port authority issue tax-exempt bonds. Other cities have explored using existing surplus city revenues, lease-back arrangements with private cable companies, revenue bonds, general obligation bonds, and loans from private lending institutions.

Cooperative Ownership

In the United States, cooperatives exist in almost every type of business. There are cooperative banks, restaurants, electric utilities, and dairy farms. In the early 1950's, small villages desiring television reception formed co-ops to divide costs and make cable TV feasible. While the co-ops usually serve rural areas, larger communities like Davis, California, are now considering cooperatives because of their democratic structure, long tradition, and philosophy of service and member benefits.

Cable cooperatives operate with the same basic purpose as other cooperatives—to make a profit for the users rather than for the investors. The members of a cooperative are both the owners and users of the service.

Since the early 1900's, cooperatives of all types have adhered to three structural principles:

1. One vote only for each member, regardless of number of shares held;
2. Capital to receive interest; and
3. Surplus-savings (or profits) to be returned as savings (or dividends) in proportion to the patronage of each individual or to be used for the general good of the members.

Cooperatives can be formed on a nonprofit or a taxable basis. Although nonprofit status offers benefits for many types of cooperatives, the depreciation allowance for the large initial capital investment of a cable system offers significant advantages for a profit corporation. Principal sources of funds for cooperatives are membership or stock sales to members. Additional sources include (a) loans from investors, banks, insurance companies, and credit institutions; (b) sale of common and preferred stock; (c) mortgage, income, and venture bonds; (d) revolving capital and capital reserves; and (e) lease-back arrangements. In addition, other existing cooperatives may be interested in investing in new cable cooperatives.

The Western Wisconsin Communications Cooperative (WWCC) in rural Trempealeu County is an example of the cooperative approach. The WWCC effort was initiated in the early 1970's by the eight county school districts, which saw cable as a way to provide agricultural, social service, and educational programming to county residents. The use of two-way

cable has reduced the need for busing students and/or teachers among schools. The system was financed through a million dollar loan from the Farmers Home Administration, a Federal agency that provides low-cost loans to various rural facilities.

Joint Ownership with a Private Company

The third public ownership model is to share ownership with a private operator. Existing models include shared ownership between a private operator and the city, public ownership with a management contract to a private company, and a management agreement that includes private investment in some of the capital expense of the system.

The Grosse Pointe, Michigan, cable system is a joint venture owned partially by a nonprofit corporation, five municipalities, and a private operator. In Paterson, New Jersey, the city will own a major part of the physical cable plant, which it will lease to a private operator who will provide a portion of the initial capital required for system construction. In Washington, D.C., the Mayor's staff committee recommended the city consider establishing an economic development corporation which would have public and private sector representation on its Board of Directors as well as combined public and private financing.

Joint ventures can be financed in a number of ways. The city can finance its portion in the same ways as it could finance a municipally owned system. The private operator can finance through existing company revenues or through private lending institutions. The percentage of ownership by participating parties varies.

The Debate

The following pages summarize the debate over public ownership but any municipalities' decision must turn on its own local needs and conditions.

Arguments in Favor of Public Ownership Models

Proponents of public ownership make the following arguments:

City Services and Economic Development

Cable systems can help deliver municipal services, from education to traffic control, and can assist in the overall economic development through services offered businesses, from teleconferencing to data transmission. Although private companies can provide the technology for such services, proponents feel that the private companies which have profit maximization, not long-range community development, as their goal will not offer the software and services a publicly owned system would.

Subscriber Rates

Existing publicly owned cable systems, whose goals are consumer

service maximization, have offered lower rates to consumers than private companies offering similar services in the same States. Cities find this an especially important consideration as they see cable becoming more of an information utility. Some cities fear that an "information gap" may develop along economic lines and that at a time when the cable industry is seeking rate deregulation, publicly owned systems may provide an effective means of ensuring affordable rates.

Local Ownership

The ownership structure of the cable industry is undergoing rapid change. In 1970, broadcast, telephone, publishing, program production, and distribution companies owned 49 percent of all cable holdings. By 1980, this proportion had increased to 72 percent. Thus, most local cable systems now are being run by national media conglomerates.

Apart from the dramatic reduction in local ownership, this change means that cities often deal with one set of company staffers during the franchising process and another set for system operation. Some cities are concerned that promises made during the franchise bidding will be abandoned later as the corporation's motivations change from winning the franchise to maximizing profits.

In addition, proponents are concerned that a concentration of ownership and a cross-ownership situation will reduce the diversity of information available to the public. Many cable systems are owned by the same corporations that provide the leading programming services. These companies may discriminate against competitors' services.

Proponents believe that public ownership models offer a solution to these problems because they provide local control and accountability and because the owner has no economic interest in programming.

Jobs and Revenues

Economic problems and Federal cutbacks have left many cities with fewer job opportunities for residents and reduced services. Cities must seek new sources of jobs and revenue. Proponents feel that cable can provide these new sources as well as cost savings by making possible more effective delivery of many city services. Private companies usually bring in personnel from other systems, while publicly owned systems hire local residents and thereby offer new job opportunities to the local community. Return on investment in cable varies widely, with some companies realizing an 18 percent return and others realizing over 60 percent. Public ownership, with its reduced financing costs, would produce substantially more revenue than a 5 percent franchise fee paid by a private company.

Promise versus Performance

Many cities feel that the cable industry's performance has not matched its contractual promise. Cities served by a variety of companies

have had problems with construction in underground and low-income areas, signal strength and leakage, billing practices, and provision of promised access facilities and staff. Proponents feel that publicly owned systems, having a consumer orientation, would provide better quality service.

Arguments Against Public Ownership Models

Opponents of public ownership make the following arguments:

System Financing

The capital intensive nature of cable and short-term operating losses require a substantial initial investment. Critics of public ownership feel that publicly owned systems may be delayed or prevented from raising the required capital because of bond issuance requirements, questionable bond marketability, or poor credit ratings. Tax advantages and the availability of internal capital and debt financing is considered a major advantage of private ownership.

Recent changes in Federal tax law offer private industry tax credits for operating losses and allow accelerated depreciation on capital items. These benefits are not available to alternatively owned operations unless they are joint ventures with a private company or have lease-back agreements. Opponents feel that these tax advantages outweigh the lower lending rates municipal systems may be eligible for through municipal revenue bonds and other revenue sources.

Risk

The multichannel systems now being constructed require huge initial investments, and their financial health depends on a level of public demand for cable services. Since the level of demand in major markets is not yet proven, critics argue that there is a considerable element of risk. Some cable industry representatives feel that cities should leave the risks to private companies and not place the burden on the public since cities can share in some of the rewards through franchise fees.

Government Competition with Private Industry

Opponents of public ownership argue that public entities should not perform a service that private entrepreneurs are willing and able to perform. They also point out that a municipally owned cable system may have unfair advantages in competing with other private media, such as broadcasting and newspapers.

Expertise

Opponents of public ownership feel that cities and other alternative entities will be unable to attract the fiscal, management, and engineering expertise required to own and operate cable systems. They believe that this

lack of expertise, stemming in part from lack of career advancement opportunities and lower salaries, will result in poorly constructed and maintained systems that offer less service to subscribers.

Government Control of the Media

Municipal—as opposed to cooperative—ownership raises the concern that programming may be biased to favor incumbent city officials or censored to reflect their program preferences.

Numerous court decisions have held that public ownership of an electronic media system does not violate the First Amendment, and courts have specifically upheld municipal ownership of cable.

Moreover, public ownership may raise antitrust dangers, especially in light of the *City of Boulder* decision. If a city decides to provide its own cable TV service and exclude private competitors, it might be charged with intent to monopolize under the Sherman Act. The risk is greater than in the case of a single franchise to a private company because the city may appear to be favoring itself. However, there have been no cases holding public ownership arrangements illegal. The outcome would depend on the particular case, and public ownership very likely will be upheld in many situations.

Summary

If a city is looking at public ownership, it should consider carefully the differences between the three models. The advantages and disadvantages listed above apply differently to the different models. Cities that are interested in public ownership options also should conduct a thorough analysis of the area, including technical, financial, legal, and structural issues. The decision should depend on local conditions, the State and local legal structure, and on the community's priorities for its cable system.

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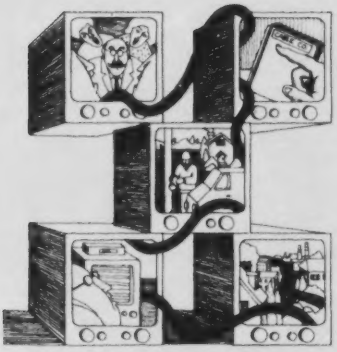

Rate Regulation

By

Deborah Love-Heilig

Chapter 7: Rate Regulation

Municipalities frequently receive requests from cable operators to increase the basic monthly subscriber fee. The decision whether to allow such increases is one of the more complex regulatory issues in cable television. In evaluating the reasonableness of a rate increase request, the local government must resolve issues that run the gamut from philosophical considerations (for example, whether the level of rates is better left up to the marketplace) to practical operations (for example, what items to include in the rate base). Rates must be balanced against the quality of service, the expectation of cable's potential development, the necessary opportunity for the cable company to earn an adequate rate of return, and an assurance that subscribers are not paying excessive rates.

Rate regulation is not mandatory for local governments. The Federal Communications Commission (FCC), in July 1976, amended its rules deleting the requirement that local governments regulate rates.[1] In so doing, the FCC noted that some State and local laws do not provide for such regulation, and it felt that non-Federal authorities should decide themselves whether to regulate.

If a local government does regulate rates, its authority is limited to oversight of basic service charges. The FCC has preempted the regulation of pay cable rates.

The Decision to Regulate Subscriber Rates

Some local officials leave cable service prices to the marketplace—they rely on market supply and demand to set the "optimal" price or rate for cable service. Others feel that the classic free market approach does not work because cable exhibits the characteristics of a monopoly; that is, the operation can charge rates that are too high, which can lead to excessive profits for the operator, inefficient resource allocation, and financial hardship for consumers. A few States have classified cable as a form of public utility and imposed detailed rate regulation. Most States, however, have left the decision to regulate rates to local governments.

Cable television shares many of the economic characteristics of regulated industries; for example, it benefits from economies of scale, and it requires expensive, highly specialized plants and facilities. Once built, a cable system can add new services at very low incremental cost, so duplication of facilities by direct competition is highly unlikely. These characteristics, however, do not automatically require governmental regulation so long as there is substantial consumer discretion in whether or not to subscribe. Most regulated industries provide a service or produce a good that is a "necessity" for which consumers have no readily available

[1] Report and Order (Docket 20681), 60 F.C.C.2d 672 (1976).

substitute. Examples include telephone service, water, power, and public transportation.

So long as cable television retransmits broadcasts and material that can be received by other means, cable cannot be considered a necessity. In many communities, however, television reception is poor without cable service. People depend on television for information and entertainment. When cable television is introduced in areas without strong over-the-air television signals, market penetration rates (the number of actual as compared to potential subscribers) often exceed 80 percent of all households. In such situations, the operator can be described fairly as providing an essential service.

Thus, by observing penetration rates as cable matures in a community, local officials can evaluate the degree to which local citizens depend on the local system for essential information and communication services that require regulatory assurance of fair prices for quality service.

Systems Under Construction

Most cable systems do not achieve their maximum penetration level until at least three years after construction is completed. Consequently, rate regulation of systems under construction or recently completed may not be warranted, particularly if they are suffering initially from low penetration. Such forbearance may give a system time to develop a marketing effort to increase penetration levels.

Some localities have encouraged low rates without direct rate regulation of new systems by allowing proposed rates to become the most important consideration in evaluating franchise bids. Because the bid process is competitive, this approach is one way to allow market forces to establish supply prices, at least in the early years of the system. But some observers have argued that cities awarding franchises to the applicant promising the lowest rates ignore the complexities involved in cable operation and financing that may cause higher rates later. Some cities have sought to minimize this problem by including in their request for proposals provisions stating that preference will be given to applicants who offer the most reasonable rate schedules that are also cost justified. Usually, such preferences are available only if the applicants make guarantees that they will not request rate changes for three years. In addition, as a measure to insure a cable operator's compliance with its proposed construction schedule and service offerings, some cities have requested that cable operators agree not to increase rates until the system is constructed.

Even analysts who advocate a "hands-off" approach to rate regulation of systems under construction suggest that local officials should initiate rate oversight and review procedures during a system's formative stages. Any eventual rate regulation will be facilitated if financial data are collected from the beginning. Many cities require system operators to submit detailed annual reports for review by the franchising authority. The uniform ac-

counting standard adopted by the FCC in its annual cable financial report form (Form 326) is a possible model for such reports.

Low-Penetration Systems

Typically, cable systems with low penetration levels (less than 35 percent) are found in urban areas where residents are already adequately served by over-the-air broadcast signals. Some analysts have cautioned that local officials need to be aware that consumer demand in areas of low penetration is so price-sensitive that any rate increase, even if justified by a rate-of-return analysis, may actually reduce the system's overall revenues. If such a posssibility exists, these analysts suggest that the best regulatory approach may be to deregulate the rates and let the system operator set the price and service offerings. The operator will usually increase service offerings, engage in more promotion, and offer price incentives in hopes of increasing subscribership and ultimately revenues. In allowing operators such discretion, local officials should put the operator on notice that once penetration exceeds a predefined threshold, some form of rate regulation may be imposed.

Medium-Penetration Systems

Analysts suggest that appropriate control of systems with penetration at the lower end of the scale (35 percent to 75 percent) may amount to nothing more than a detailed review of financial statements to insure that the system's subscribers are fairly treated. As penetration increases, a more elaborate plan of rate regulation can be developed and implemented.

According to these same observers, a system experiencing a penetration rate of close to 75 percent is probably the most difficult type of system to regulate because it is probably in a position to exercise monopoly pricing power and take advantage of its subscribers. On the other hand, market share or penetration rates do not necessarily provide market power to set prices. For example, the cable service may be so underpriced that consumers see it as the best way to spend their entertainment dollars. The important issue is the extent that penetration will vary with prices. That "demand curve" relationship defines the cable operation's monopoly pricing power. The regulatory framework selected must reflect these differences. Accordingly, local authorities may want to take a flexible approach that allows solution of current problems but does not prejudge the long-term price structure of the system.

High-Penetration Systems

High penetration systems (greater than 75 percent) normally exhibit strong inelasticity of demand; that is, their customers will be less likely to terminate service in response to rate increases. In such systems, profit levels are generally high and the financial risk to the operator is low. Analysts suggest that in these systems rates should be regulated and based on net invest-

ment in plant to prevent operator complacency. Net investment in plant is defined as the value of the capital investment in the cable plant less accumulated depreciation.

The regulatory procedure developed by local officials should be tailored to the specifics of each cable system. A system with low penetration levels may warrant little or no rate regulation. Conversely, systems experiencing heavy market penetration may require a high degree of regulatory overview to insure that subscribers are not providing the operator with excessive profits. Local officials should also keep a watchful eye on the operator's compliance with the cable ordinance. An operator's failure to fulfill the commitments of the ordinance without reasonable cause may be just cause to deny a rate increase.

A well-developed and clearly defined regulatory procedure is essential for local authorities and can minimize the risk of legal battles with the cable operator. Courts will overturn a regulatory decision made by a local authority if it is found to be arbitrary. A clearly stated, predefined procedure like that presented in the following section may help local authorities avoid such reversals.

Establishment of Regulatory Procedures and a Fair Rate-of-Return

Once local officials decide to evaluate a proposed rate increase, the first step will be to determine a fair profit margin for the company. This task is one of the more difficult regulators undertake. The most common method is based on the company's rate of return. Rate of return is a profitability ratio expressed as a percentage that compares earnings to investment. There are several ways to calculate rate of return, but the most common method used in public utility regulation is based on net investment. It relates before-tax net income (the return to the equity investors; that is, the stockholders) and interest expense (the return to the debt holders or banks) to the net investment (the undepreciated book value of the system's capital assets). This net investment is called the "rate base."

Normally, a rate of return on net investment is adequate if it covers the combined costs of the capital invested in the system. For example, if the capital funds used to construct the system were 50 percent from loans at a 15 percent interest rate, then the cost of debt capital is 15 percent. If the required return to the shareholders or equity investors is 20 percent, then the cost of equity capital is 20 percent. An adequate allowed rate of return on net investment to the operator would then be 17.5 percent—the weighted cost of its invested capital. An allowed rate of return is not a *guaranteed* rate of return; it merely establishes the ceiling on a company's net profits. Poor management, bad service, and bad economic conditions may all prevent the company from earning its full permitted profits. Establishing an allowed rate of return that is higher than needed may permit unnecessary windfall profits for system owners. Establishing an allowed rate of return

that is too low will make it difficult for the system to obtain new sources of capital for plant improvement and may cause financial difficulty for the operator. Within this framework of maximum possible profits, individual rates must be set as part of the overall rate structure to enable the company to earn revenues that do not exceed the allowed rate of return. This is the company's revenue requirement.

Determination of the Revenue Requirement

The basic function of rate regulation is to determine the revenue requirement of the operator. The operator may set rates so as to generate sufficient revenues to (a) cover all costs associated with the operation of the company and (b) yield an allowed rate of return on the operator's invested capital in the business.

The first step in determining the revenue requirement is to ascertain all allowable operating expenses, including wages, salaries, benefits, maintenance, depreciation, interest, and taxes (not including income taxes). If a procedure for reporting this information is set up at the inception of the franchise, determining expenses is a fairly easy task; otherwise, all financial information supplied by the operator should be documented by audited financial statements.

Second, the net book value or net undepreciated investment in the cable plant should be determined. Net investment is simply the book value of capital assets and can be determined by subtracting accumulated depreciation from the total value of tangible property. Net investment serves as the rate base under this method of regulation. Multiplying the rate base times the established rate of return (expressed as a percentage) yields the permitted return on the investment. The interest expense is subtracted from this figure because it represents the return already paid to the investors of debt capital. The resulting dollar figure is the allowed net income to the cable company's owners either in the form of dividends or as profit to a partner or sole proprietor.

To determine the amount of revenues needed to generate this net income, all allowable operating expenses are simply added back. If total expenses plus allowed net income exceed the total revenues possible under current rates, then a rate increase may be justified. If the total revenues projected by the operator exceed total expenses plus allowed net income, a rate reduction may be in order.

Control of the Rate Structure

If a cable company offers only one tier of basic service, the monthly subscriber rate can be calculated by dividing the overall monthly revenue requirement by the number of anticipated subscribers. In reality, most cable operators receive revenues from a variety of additional sources, including fees for pay programming and charges for installation, second sets, and reconnection. To arrive at a necessary level of revenue requirement per

basic subscriber, all these other anticipated fees must be deducted from the annual revenue requirement before dividing that figure by the number of anticipated subscribers to the basic service. When a cable company offers more than one tier of service, any percentage increase that is justified by these computations can be apportioned among the subscribers in the different tiers according to their representation in the total subscriber revenue pool.

Issues in Applying Rate-of-Return Regulatory Methodologies

Accounting Definitions and Structures

Accurate records of revenues, operating costs, depreciation, and investment are critical to determining the overall revenue requirement. Accounting standards are also necessary to distinguish between investments in capital assets and expenditures relating to the cost of doing business. Without these standards, earnings can be inflated artificially by charging operating expenses to capital accounts (thereby increasing the investment upon which the return is based), or they can be understated by charging capital expenditures to operating expenses. Accounting standards should also be used to insure that the company's asset account is accurate, because regulated companies earn a return based upon their useful investment.

Finally, a uniform set of accounts is needed to separate regulated and nonregulated revenues and costs. A clear distinction must be made between the regulated components (basic service) and the unregulated components (pay service) to allow an accurate determination of the basic service revenue requirement and to prevent cross-subsidization of the unregulated portion.

Determination of Capital Structure

The overall relationship between debt and equity has a significant impact on the cost of capital. Increases in the percentage of debt within the capital structure cause the overall cost of capital to decline because the allowed investor return will normally be higher than bank lending rates. Excessive debt, however, may make it difficult for the company to raise additional capital and may make the company too sensitive to changes in interest rates and economic cycles.

Regulatory authorities generally try to require a capital structure for the regulation enterprise that will insure financial stability. If regulatory authorities or lending institutions imposed no restrictions or controls, entrepreneurs would be tempted to maximize the debt portion of their capital structure because to do so would minimize the risk of losing their own money should the venture fail. In addition, interest is an expense item that can be passed through to subscribers and deducted from taxable income.

Measurement of Efficiency

Local officials may often consider rate increases as an incentive for

companies to operate more efficiently. Several methods are available for measuring operator efficiency.

One way is to compare data for the particular system with national data. By developing comparative ratios such as operating expense per subscriber or the relationship between revenues and expenses and evaluating system ratios against national or regional ratios, a municipality can estimate whether the system is operating as efficiently as other similar systems. If it is not, local officials could consider rejecting rate increases until the system improves its operating efficiency.

Overhead

Another difficulty that often arises is determining the validity of overhead costs when the cable operator owns and operates several other systems. Multiple-system operators (MSO's) provide certain centralized services such as billing, legal and accounting services, lobbying, and purchasing and charge each individual system for these services (commonly called corporate overhead). Often this charge is not calculated on the basis of actual services rendered; instead, the entire corporate cost for services is apportioned among the systems based on the number of subscribers or gross revenues they contribute to the MSO's operations.

Municipal officials often question whether these overhead charges are justified or whether local subscribers are subsidizing the construction and operation of other new systems or contributing unwarranted profits to the parent company. Municipal officials can take several approaches to deal with these concerns. They can estimate the direct cost for those services provided by the parent company and compare this estimate with actual pro rata allocations. If the estimates are higher than the pro rata allocations, the officials could use the actual overhead costs in their rate analysis. Alternatively, the officials could request a breakdown from the parent company of all overhead costs and an explanation of how these costs are allocated to the local system. Based on this showing, the officials could accept certain costs and reject others.

Rate Increases for Multijurisdictional Systems

Regulatory problems also occur when a municipality shares a common cable system with surrounding communities. These systems typically share common facilities such as headends, cable, personnel, and office space. Allocating capital and operating costs among each political jurisdiction is an almost impossible task. Unless a detailed and exhaustive review of current practices and procedures is made, any allocation is somewhat arbitrary.

For example, one easily administered approach allocates costs based on the number of subscribers served by the cable system; however it ignores factors such as the density of homes per mile and incorrectly assumes that subscribers contribute equally to operating costs. (The higher the density,

the lower the operating cost per subscriber.) Another frequently used allocation formula compares the number of miles of plant in a city to the total miles of plant throughout the system, but it incorrectly assumes that maintenance is equal for all components of the cable system. This approach ignores that new cable generally requires less maintenance than old cable as well as the fact that some facilities may be shared.

Thus, any localities with systems owned by common operators should consider conducting a joint rate investigation. In any event, communities should try to agree on some arrangement that avoids the improper allocation of costs.

Summary

The application of rate regulation is complex and difficult. Many specific issues must be clarified and resolved before the process can be undertaken. Unless plans and procedures are clearly spelled out, the operator and local officials run the risk of having their actions challenged in court.

Depending on local circumstances, rate regulation may not always be the preferred alternative. The use of rate-of-return regulation (or any other approach that places limits on the profitability of a company) implies that the cable system closely replicates the characteristics of "natural" monopolies, a similarity that does not always exist. To impose rate-of-return regulation on cable systems with low penetration may do more long-term harm than good. If a system with low penetration is underserving its market, it may suffice to let the marketplace determine the reasonableness of rates.

When rate authority is exercised, increases should be given to encourage and reward operators who provide efficient, quality service. When considering a request for an increase, local officials should verify that the quality of service that was stipulated in the franchise agreement is being met. In addition, any long-term regulating framework that officials establish should require that complete and valid financial information be filed on an annual basis. Consideration also should be given to incorporating a rate review process in the local ordinance. This, combined with annual reports, will insure the availability of both an agreed-upon procedure and enough information to act on rate increase requests.

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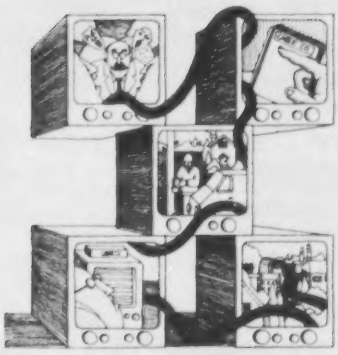

Franchise Enforcement And Administration

By
Merry Sue Smoller
Nancy J. Jesuale

Chapter 8: Franchise Enforcement and Administration

In the past, local governments have invested little time and resources in franchise enforcement. Older franchise agreements and ordinances frequently lack or are nonspecific about enforcement provisions and service standards. Often, cable companies have not constructed systems in a timely manner or provided the level of services promised. The disappointing performance history of some cable companies has prompted growing local government interest in effective enforcement. This interest has also been spurred by the withdrawal of the Federal Government from the cable policy arena. Moreover, as larger urban areas finish long and arduous franchising processes, their interest turns more and more toward insuring performance and compliance with the franchise agreement.

Today, when local government budgets are strained, the term "cable franchise" is almost always preceded by the adjective "lucrative." In most markets, the cable system operates as a monopoly. Therefore, the local regulator has an important function: to create a regulatory structure to compensate for the lack of marketplace competition, and to administer these regulations in a fair manner.

It should be emphasized that no local government has to award a franchise for cable service, nor do officials have to award just one franchise. The history of the industry, however, indicates that a community that desires cable normally will not have the opportunity to develop two competing cable systems. "Overbuilds" generally have been unsuccessful. Thus local governments usually reserve the franchise award for the operator who commits to building what appears to be the best cable system for that community.

Ideally, provisions of the ordinance and a contractually binding franchise agreement between the local government and the selected company cable operator should allow local decisionmakers to "franchise and forget." In reality, continuing involvement is usually necessary. The pressures of the competitive franchising process often leads to promises to provide costly services that have little revenue potential, such as local programming, services to areas of low population density, free or low-cost service to nonprofit institutions, and costly access facilities. After the franchise award is made, however, the operator will focus on building a system and making a profit and may be reluctant to deliver these non-revenue-producing services. Therefore, some continuing regulatory oversight is necessary to insure compliance.

Enforcing and Monitoring a Franchise Agreement

The regulatory or franchise ordinance (discussed in chapter 4) is the basic tool for franchise enforcement. The ordinance sets forth the rights and responsibilities of both the city and the cable operator and the rules under which the system will operate. Although the ordinance provides the

basis for enforcement by establishing standards, requiring reports, and specifying penalties for noncompliance, administrative procedures must be developed to implement its provisions as well as those of the franchise agreement.

The chief function of the franchise administrator is to monitor compliance. The administrator needs to develop a method of obtaining the information necessary to compare the cable operator's performance with the provisions of the ordinance and the franchise agreement. If this monitoring process reveals that the franchisee is in noncompliance, the cable administrator must determine the appropriate remedy. This remedy may be a recommendation to the regulatory body, usually the city council, that a provision of the ordinance or agreement be waived, that penalties be applied, or that the franchise be revoked.

To establish an effective system of monitoring compliance, the administrator may begin by compiling an outline detailing construction deadlines, equipment delivery schedules, planned delivery dates of new subscriber services, and so forth. In conjunction with reports filed by the cable operator, the outline is an aid in keeping track of the franchisee's compliance with required timetables.

The cable administrator should develop detailed reporting forms to obtain precise information from the cable operator. For example, to verify that the city is receiving the full amount permitted under the franchise fee stipulated by the ordinance, the administrator must have an exact accounting of subscribership and revenues.

Monitoring system construction is not only important during the initial construction phase, but also in later years as service is extended to new subdivisions and to homes in outlying areas. Report forms should contain, at a minimum, the number of miles, specific areas, and number of houses passed and homes installed each month. The franchisee should provide evidence that all necessary construction approvals and permits have been obtained, as well as assurance that required standards for construction and public safety are met continuously. In the case of construction and public safety standards, the city may wish to conduct on-site inspections to verify that the franchisee's reported statements correspond to actual practice. Upon activation of the system, the city will want the cable system operator to conduct initial proof-of-performance tests to confirm that the technical performance specifications promised are actually being delivered. Annual proof-of-performance tests submitted to the Federal Communications Commission by the system operator should also be submitted to the city. The city's administrative authority may wish to use hire a professional engineering consultant to assist in technical reviews. Indeed, in the event of disputes in areas requiring professional expertise, independent verification is often the only practical way to determine performance compliance.

One way to assure compliance and mutually beneficial cooperation between the city and the cable system operator is to demonstrate willingness

to enforce through comprehensive and precise administrative procedures. If a company perceives that the ordinance and franchise agreement cannot be circumvented, it may be less inclined to cut corners. Moreover, since disagreements between the cable system operator and the city are bound to occur, and since some disagreements may end up in court, the city's case may rest on the extent to which it has compiled accurate and detailed supporting documentation.

The foregoing discussion of enforcement procedures is predicated upon the locality having strong enforcement provisions in its ordinance. However, many localities have ordinances or franchise agreements that do not provide effective enforcement mechanisms. For example, the ordinance may lack specific penalties, short of franchise revocation for noncompliance, or its language may be ambiguous, leading to disagreement over interpretation. If the ordinance can be amended, such deficiencies should be corrected. Care must be taken, however, that any amendments do not alter the rights granted to the system operator under the franchise—such alterations can be made only with the operator's consent.

A request from the operator for a rate increase, franchise extension, or renewal may present the opportunity to negotiate an improved franchise agreement. These improvements might include an updated ordinance, improved system performance standards, stronger enforcement provisions, or an agreement to provide new services.

Administering the Agreement

A recent national survey indicates that the development of more specific ordinance provisions and oversight procedures has yielded a variety of administrative approaches.[1] The size of the local government, the amount of money available for cable enforcement, and the sophistication of the cable system directly affect which approach is chosen. Of the respondents to the survey—individuals responsible for local telecommunications planning and regulation—approximately 30 percent reported yearly budgets of less than $50,000, and 25 percent have yearly budgets between $250,000 and $1,000,000.

Administrative budgets often are determined by the amount of franchise fees paid by the cable system operator. The proceeds from this fee may fund not only cable regulation, but also other cable-related expenses such as municipal access programming, delivery of municipal services using the institutional network, and support for community access programming. Large cities usually need extensive cable oversight and frequently establish a telecommunications or cable office with a full-time staff. Smaller jurisdictions, which have less money available from franchise fees, most often use advisory committees or existing departments or staff to administer

[1] Barry M. Orton and Hans Giesecke, *Municipal Telecommunications Officers: A National Survey* (1981 annual conference of the National Association of Telecommunications Officers and Advisors, Boulder, Colorado).

regulatory policies.

Although approaches to franchise administration and enforcement vary from city to city, some basic models can be identified for descriptive purposes: (a) the cable or telecommunications office, (b) the advisory committee or regulatory commission, (c) an existing agency or department, and (d) professional consultants. Most localities use a combination of these, notably a cable office working with an advisory committee, or an existing city department working with occasional help from a consultant.

The Cable Television or Telecommunications Office

Many large cities with new cable systems have established special cable television offices to handle enforcement, government programming, complaints, public information, and planning. Such an office usually is staffed by at least one full-time professional employee who maintains contact with offices in other jurisdictions and monitors cable policy and related developments. The staff, working full-time on cable matters, can develop productive relationships with the system operator and with community groups interested in cable uses. Such offices usually report to the mayor or the city manager, although some report to the city council. Frequently, they work with or provide staff assistance to an advisory committee or regulatory commission that reviews local cable policy.

The Advisory Committee or Regulatory Commission

The cable advisory committee model is a common administrative approach, found in both large and small cities. It is usually established by ordinance as an ongoing advisory group mandated to oversee regulatory policy set forth in the ordinance, to report to the city council on policy recommendations, and to review required reports submitted by the cable operator. Often, advisory committees facilitate the development of local programming, helping to establish access channel policies and to resolve disputes. The members are usually appointed and serve as volunteers.

If the members of the advisory group have a stake in effective cable enforcement, they may be more successful as franchise administrators. Therefore, representatives of different subscriber or user groups, such as minorities, senior citizens, handicapped persons, the business community, or the arts, may be appointed. Other selections may be based on expertise, reserving specific positions for an educator, accountant, communications specialist, or engineer. The committee's chances for success will also be improved if it has staff support to handle routine administrative functions. If provisions of the ordinance need enforcement action, the advisory committee must usually take the issue to the council or the mayor for direct action.

The regulatory commission differs from the advisory committee because the city gives it actual regulatory authority. Such commissions may have quasi-judicial powers, with the authority to hear complaints, issue

findings, and assess penalties for noncompliance with the terms of the ordinance. The commission may be constituted as an independent authority, with separate staff and budget.

In several areas, cities, counties, and townships have worked together during the franchising or franchise renegotiation process to develop a common cable system that serves several jurisdictions under one contract or identical contracts. In some of these joint franchise agreements, regulatory authority is returned to the individual jurisdictions, although a joint committee may be formed strictly for advisory purposes. Other joint agreements have established joint regulatory commissions or independent authorities for continuing enforcement and administration. Retaining such a joint regulatory effort may allow administrative economies, establishment of consistent service standards and rates, and cooperative management of system expansion and development.

An Existing Agency or Department

Many localities place ongoing cable franchise administration in an existing agency, such as the city manager's office or the planning department. Others may assign tasks to several offices. For example, rate reviews may be handled by the finance office, and programming oversight by the library or public information office. If an existing agency performs franchise administration, its duties and responsibilities should be clearly delegated so that the public, other city departments, and the cable system operator know exactly whom to call when questions or problems arise.

If lines of responsibility are clearly drawn, using an existing agency can provide a sensible solution for localities that do not have the budget resources to create a new agency devoted to cable television administration. A further advantage is that an existing agency has established working relationships with other components of the local government.

Professional Consultants

Whether a community uses an advisory committee, an existing department, or a new cable office, it may want to use outside consultants to deal with specific technical, financial, or legal questions or to provide data on experience of other cities. The volume of cable administrative tasks fluctuates, and the use of outside consultants on an ad hoc basis allows a city to deal with cable matters without hiring extra staff or overburdening existing staff.

Summary

Whatever approach is chosen, the city should implement well-defined procedures for administering the franchise. Consumers, city agencies, and the cable company should know where to go to get information about the franchise. Public files must be maintained, and processes for resolving complaints and conducting reviews should be established. Lines of

authority need to be direct enough to identify the office or person responsible for any particular problem. Because administration of the cable franchise may involve more than one city agency, regulatory efforts must be coordinated.

Interest in cable franchise enforcement and administration has increased dramatically in recent years, prompted by new technology and services and by legislative and judicial steps to deregulate the industry at the Federal level. Local enforcement begins with strong provisions in the ordinance and franchise agreement to compel compliance by the cable operator. Clearly defined administrative procedures, including continuous monitoring and reporting, are necessary to insure that the provisions of the ordinance and franchise are implemented.

The administration of the franchise can be vested in a cable or telecommunications office, an advisory committee or regulatory commission, or an extant city agency or department. Many cities use a combined approach and frequently employ professional consultants to supplement their own staff efforts. Cable enforcement and administration are relatively new areas for cities, and as cable administrators gain more experience, they undoubtedly will develop other innovative methods of administering and enforcing franchises. As a result, a locality's prospect of receiving what the cable operator has promised will be improved, and the right of subscribers to receive high-quality service at reasonable cost will thereby be protected.

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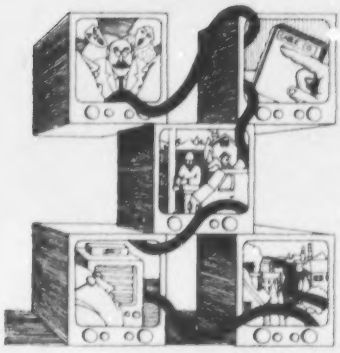

Renegotiation Of Cable Television Franchises

*By**
Nancy Jesuale

*The author gratefully acknowledges the contribution of Harold E. Horn on this subject.

Chapter 9: Renegotiation of Cable Television Franchises

Although cable systems with 52 or more channels are considered to be state of the art today, the vast majority of cable systems offer 12 or fewer channels of service, limited in many cases to local broadcast signals; one pay and/or one superstation; and a weather and time channel. By the mid-1980's, franchises for many of these systems will expire and their operators will need to ask local authorities for extensions. Most likely, authorities who have kept abreast of recent developments in cable services and technology will not be content to automatically renew the franchises of operators who merely propose a continuation of 12-channel cable service. The franchise renegotiation process offers local officials an important opportunity to contract for new, comprehensive cable communications systems for the coming decades.

The city cannot, however, renegotiate a franchise effectively without a thorough understanding of the technological and economic climate of cable. Decisionmakers need accurate information on the state of the art of cable services in general, as well as knowledge of services in geographically comparable cable markets and information on realistic needs locally. Decisionmakers should begin collecting information at least three years before a franchise expires to allow enough time for a comprehensive review and systematic renegotiation process. This lead time should minimize the risk of a loss in service or adoption of an unsatisfactory agreement. Local officials should also remember that a franchise agreement can be renegotiated at any time. It is not necessary to wait until expiration if both parties are agreeable to renegotiation or, in some cases, if the company has requested a rate increase or some other fundamental change in the agreement. Many companies prefer to negotiate an extension early in order to obtain additional financing or to justify the risk of proposed investment in new plant.

Deciding to Renegotiate or Request Competitive Bids

Cablevision magazine, in a June 1981 article on refranchising, pointed out that multiple-system operators (MSO's) are generally unwilling to bid for another operator's system. The prospect of competitive bidding introduces a tremendous amount of risk. If a company cannot reasonably expect franchise renewal, it would face great difficulty in attracting financing and would have little incentive to invest in rebuilding and upgrading. Localities interested in requesting competitive bids upon the expiration of a current franchise may find little, if any, serious interest from potential competitors of the current operator. In fact, there seems to be a "gentlemen's agreement" among MSO's not to encourage competitive bidding at the end of one company's franchise period.

If the original system operator was not doing an adequate job, however, most local officials will not rule out an alternate service provider. Most local officials, though, will start from the premise that they should

seriously consider the current company for renewal, particularly if the system has been adequately maintained and upgraded and the operator is cooperative in renegotiating. Most officials find they have good negotiating leverage with the existing company because it wants to keep the franchise, has come to expect system upgrades as a fact of life, and will be able to refinance once the company has obtained a long-term franchise extension. In the event that the present system owner refuses to negotiate in good faith, the officials can increase their leverage by raising the possibility that they may request competitive bids from other companies.

Continuity of service is an important consideration in the decision to renegotiate or open bids. An upgrade or rebuild of a system generally takes longer than new construction and must be done in phases to avoid loss of service and to allow the operator to pay for the purchase and installation of new plant. The existing operator already has pole clearances and permits, an established subscriber base, and a regular source of revenues.

If a new company takes over the original franchisee's plant, it faces the problem of purchasing and salvaging useful portions of the old plant. Some parts of the system will have to be torn down and rebuilt completely, requiring in some cases new pole permits or even new poles. Buy-out of the old system can require detailed negotiations between the two operators and the city and may cause service interruptions.

Local officials should also realize that marketing factors may affect a potential applicant's interest in bidding in a "settled" market, that is, one that has been receiving service. A new applicant may not be able to sell enough cable service to a sufficient number of new subscribers to justify the investment in new plant capacity. Industry analysts agree that a new market that has never received cable service will experience more initial consumer demand for multiple pay services and expensive interactive and text services than a market in which consumers have had limited exposure to a lower grade of cable service.

Certain circumstances, however, may prompt local officials to request competitive bids rather than renew the franchise of the existing operator. These include past animosity between the local government and the operator, the operator's unwillingness to provide adequate service or to give technical and financial information about the system, and the operator's refusal to upgrade. Faced with any of these problems, local officials can and should find another cable operator through either the competitive bidding process, a system sale, or negotiation with a potential new operator.

The Renegotiation Process

Once local officials have decided to renegotiate, they should begin a comprehensive process that involves an examination of the present system's finances, economic worth, technical status, and capability; ascertainment of any new services needed or desired over the next franchise period;

analysis of the present ordinance and franchise agreements for problems or omissions; and public input and dialogue concerning future cable services, especially if access and local origination services are desired but unavailable.

Often local officials use outside consultants to help collect and evaluate financial and technical information on the existing system and to evaluate future projections for revenues and services. Many officials also appoint a citizen's advisory committee or task force to compile information on community needs and the state of the art and to make recommendations. The beginning of the renegotiation process is also an appropriate time to involve educators, health professionals, access groups, arts councils, and other potential programmers or users of the system so that they can learn more about cable and make their needs known to officials. This kind of participation also will help the operator determine which new services are attractive to consumers and how much they would be willing to pay for them. Early public involvement in the process increases the likelihood that consumers will understand and accept future changes in cable prices and service.

The overall system review can be divided into several key review areas: regulatory, services, technical status, and financial.

Regulatory Review

Local officials will need to perform a comprehensive ordinance and contract review. During this review, they should look for problems not addressed by the original ordinance that need correcting. These problems may involve line extensions, underground policies, rate of regulation, penalty provisions, bonding provisions, technical standards, performance evaluations, financial audits, continuity of service, franchise fees, privacy, access and other services, and the provision of institutional networks. This review also will entail studying other localities' ordinances and contracts and examining recent changes in Federal and State laws concerning cable. In most cases, the original regulatory and franchising ordinances will require substantial amendments. Officials in communities ready to renegotiate may find that they are unaware of recent modifications of Federal Communications Commission (FCC) regulations, such as the elimination of access requirements. For information on these changes, local officials could contact the FCC, the National League of Cities, or the Cable Television Information Center. (See appendix 1 for a listing of organizations.)

Local governments should also review their own regulatory track record and procedures. Have they enforced the franchise provisions? Established a fair way to deal with rate requests? Performed periodic reviews of performance? Assisted when necessary with pole clearances and easements? Allowed consumer input? Been effective regulators? If officials find that they are unsatisfied with their past performance, they may want to consider establishing a new system to enforce and administer the cable ordi-

nance and franchise agreement. Such a system may involve either making an existing administrator responsible for the job, establishing a new cable office, or using an ongoing citizen's advisory committee. (The issue of franchise administration and enforcement is discussed in chapter 8.)

Services Review

A services review should address several points including the following:

1. Has the cable operator been cooperative and supportive of public and educational users of the system?
2. How do performance and services measure up to initial promises?
3. What has been the nature of subscriber complaints and how has the cable management responded to justified service and billing complaints?
4. Was the cable system constructed in a timely manner as housing density warranted?
5. Has the cable operator been innovative in providing new services as technology and subscriber interest warrant?

A service review will require examination of subscriber documentation, which is usually filed with the city and at the cable operator's offices.

This review also provides an opportunity to examine the need and demand for new services, particularly interactive services, institutional networks, educational programming, and public access. The community groups, advisory committee, and cable operator should be involved in ascertaining the need for these services. All individuals involved in the review should keep in mind that the delivery of community channels will undoubtedly require expanded channel capacity and a large new investment that must be reflected in the company's projected expenses and revenue requirements for the coming franchise term. (The needs ascertainment process is discussed in volume I.)

Technical Review

A technical review of the system should address the following questions:

1. To what extent is the system obsolete?
2. Does it require rebuilding?
3. Can a staged transition in upgrading be accomplished?
4. Have construction and maintenance procedures been up to standard?
5. Is the quality of retransmission of signals adequate?
6. To what extent have amplifiers and cable deteriorated?

The local government may want to employ an engineer or technical advisor to perform on-site tests with the cable operator's engineer and to evaluate the present condition of the plant and equipment. The evaluation should include an appraisal of the headend equipment and the quality of the

equipment and signal at various points in the system. This information will help officials evaluate the cost and extent of a future rebuild and will provide a factual basis for future negotiations with the system operator. Once a proposal for a rebuild or technical expansion has been received by the local government, a technical advisor should review the plan for the city to insure that the design is adequate, that the construction schedule is realistic, and that projected future capacity requirements are realistic.

Financial Review

An independent examination of the financial status of the existing system is essential to establish negotiation strategies and to determine feasible upgrading. Using standardized financial report forms, a community should solicit the following kinds of information:

1. What trends do historical data show about the system's operation over the past five years, including routine financial information such as itemized capital expenses, operating expenses, and general service expenses?
2. What accounting practices have been used and to what extent have they been consistently followed over the years?
3. What has been the rate of return and exactly how has it been calculated?
4. If the system is owned by an MSO, are local revenues and expenses separable and documented?
5. How do the operating expenditures compare with industry norms? Does this information indicate that the system is run efficiently, or are some expenditures unusually high in comparison with similar cable systems?

Decisionmakers should examine the financial information submitted for the proposed new franchise period to determine the following:

1. What system modernization and rebuilding is planned, at what annual cost, and on what schedule?
2. What new services are proposed, and what is their estimated impact on subscriber rates, expenditures, and revenues?
3. What is the projected rate of return, assuming any proposed system modernization and possible rate increases?

Proposal Review and Contract Development

During the system review, local officials should request a proposal from the company regarding its contract renewal. This proposal should provide detailed information about the company's proposed technical rebuild and plant expansion, new services, new rates and tiering structures, any institutional network that might be offered, and specific financial data.

The company's response should constitute a legal offer of services to the community that could become enforceable in any new contract. This proposal should be analyzed by a consultant or someone with financial and

technical expertise to see if it complies with stated community needs and if it is reasonable and comparable to bids in "new build" markets.

If the officials find that the offer is reasonable, the contract negotiations should continue. If the negotiations fail, the local government should consider soliciting bids from other interested companies.

Summary

The best way for a local government to obtain the most favorable results in a renegotiation effort is to approach the process with good technical and financial knowledge about the present system and with an understanding of the economic feasibility of proposed plans for future service. Collection of the necessary information should be started three years or more before the franchise expiration date. The renegotiation should be completed before expiration of the original franchise agreement to avoid any loss of service.

Case Histories

Austin, Texas
Population: 356,000
Cable penetration: 57 percent

Austin, Texas, has the seventh largest existing cable system in the country. The city began its renegotiation process in the summer of 1979. The franchise was not scheduled to expire until 1983, but the system operator, Capital Cable, owned by Midwest Video Corporation and the LBJ Corporation, initiated an early renewal because it planned to upgrade from 12 to 36 channels but did not want to do so until it obtained an extension of its franchise. Several months later the city council hired a consultant to perform technical and financial evaluations of the existing system and to aid in the renegotiation process.

The renegotiation process was exceptionally difficult for Austin because the company's local reputation was under attack; citizens were dissatisfied with its local management. The system, which had been established in the 1960's, offered only 12 channels. Local management had experienced growing animosity from community users of the system and from dissatisfied subscribers. In contrast, during this same period other Texas cities were receiving state-of-the-art system proposals. Austin wanted equivalent service assured in its renegotiated franchise. The city council was inundated with information on what other cities in Texas and nationwide would receive from the competitive bidding process in new markets. These factors put tremendous pressure on the council.

Community sentiment against Capital was so strong that the city might have considered taking competitive bids if the American Television Corporation (ATC) had not made an offer to purchase and improve the local system. Once the buy-out offer was made, ATC became an integral

part of the negotiation. City staff negotiated with ATC from January through May 1981. The council directed the staff to negotiate for two separate service options: a dual 330 MHz system (88 channels) and a single 400 MHz system (54 channels). The city wanted the extra capacity of a dual system but also wanted to maintain low rates. (During its franchise, Capital had never raised its $4.95 basic service rate). The negotiations involved two simultaneous bids from ATC. A specific option was to be approved after the city had seen rates and service projections for both.

During the negotiation process, the city contracted for an independent needs assessment to determine where to build an institutional network. The ascertainment did not identify the sites for the institutional system, but it did document the great interest of Austin citizens and community groups and institutions in programming on both the subscriber and institutional networks. ATC's final proposal integrated many of the ascertainment findings into its proposal for services, particularly access provisions.

In the final weeks of the negotiations, changes were made almost daily in the company's two proposals as the city and the company tried to agree on rates and services. The negotiations were intensified because the city council wanted to complete the process before the impending installation of a newly elected council. The old city council did manage to complete the negotiations, agreeing to grant a new 15-year franchise to ATC upon completion of its purchase of Capital. ATC agreed to build a 54-channel interactive system with an additional installed but inactive trunk to be activated whenever the city might deem the additional capacity necessary. ATC proposed to upgrade over five years, with 23 channels in operation by mid-1982, 36 channels by 1985, and 54 channels by 1986. The new system offers 14 access channels, and $8 million has been allocated to the operation of an independent access authority over the 15-year life of the renewal franchise.

Portsmouth, Ohio
Population: 30,000
Cable penetration: 88 percent

In 1961, Portsmouth, Ohio, issued its first 20-year cable television franchise in the form of a two-page agreement. TelePrompTer (TPT) subsequently acquired the franchise. Early in 1981, TPT requested a franchise renewal from the city, asking for a new 15-year franchise with an automatic 10-year extension period. The company's proposal to the city, accompanied by a suggested new ordinance, offered to rebuild the old 12-channel system and to upgrade a 36-channel capacity.

In many ways, the Portsmouth system typified classic cable markets. The system offered a 10-channel basic service package for $6.75, including one local origination channel, one access channel, and a premium movie channel. It experienced very high penetration due to hilly terrain and the lack of local broadcast signals. The original franchise was granted before

the advent of pay television and when MSO's were busily grabbing up "money machine" markets like Portsmouth, where a retransmission service would be in heavy demand.

When the city received TPT's renewal proposal, it hired a consultant to review the bid. The consultant advised the city to require TPT to resubmit a new, formal proposal on standardized forms to solicit information on the old system's technical status and financial performance as well as on the proposed upgrade. After the company completed the forms, the consultant reviewed and evaluated the financial information and suggested issues for the city to negotiate.

Because the system serves both the city of Portsmouth and surrounding unincorporated areas and had always kept financial records on an integrated basis, officials had difficulty isolating system distribution and overhead costs associated with the city service from those connected with the county section. The city wanted to be sure that the cost of construction conducted outside of the city and associated depreciation and interest expenses would not be subsidized by city subscribers or reflected in city rates. The consultant was able to suggest methods for separating costs. Under the terms of the new ordinance, the company will be required to segregate county expenses from city expenses in its annual financial reports. The new ordinance also provides for annual performance reviews, penalties for noncompliance, construction bonds, and an active franchise enforcement program.

At one point in the process, the city was approached by another bidder, a locally owned company that hoped to be awarded the franchise instead of TPT. To discourage improper attempts at influence peddling, the city passed an ordinance prohibiting any city council member from discussing the franchise with potential bidders and prohibiting companies from offering individual city council members any services or funds. The council members apparently were not interested in the alternate proposal from the local company and chose instead to continue their renegotiations with TPT.

Overall, the negotiations proceeded relatively smoothly. At this writing, the city and the company have agreed in principle to a contract and are completing the remaining details of the agreement. TPT promised a new, interactive, 52-channel cable system (400 MHz) built in phases. It also promised 36 channels initially and, within 18 months of the starting date, 52 channels. In addition, it will install text and interactive services.

Santa Barbara, California
Population: 73,000
Cable penetration: 80 percent

Santa Barbara, California, began its cable franchise renegotiation effort in 1979, about 2½ years before the franchise was scheduled to expire. City staff and the mayor met with representatives of Cox Cable, the local franchise holder, at the company's request. At the initial meeting, Cox in-

dicated a desire to begin renegotiating the license and upgrading to a state-of-the-art system as soon as possible. The city officials told Cox that they were unprepared to make a commitment to renegotiate and could not exclude the possibility that they might take competitive bids for the franchise.

The city staff soon decided that they needed expert advice and that they wanted to resolve the issue as soon as possible, preferably before the 1981 general election, then 18 months away. The city staff was interested in a 400 MHz system and an agreement that would include an option for periodic performance reviews. After talking with a consultant, the local officials agreed that if Cox's new proposal were responsive to local needs, they would prefer working with a known entity.

The staff prepared a negotiating plan that requested that Cox submit a proposal for a new franchise within 45 days and prepare detailed information regarding the new system's design and cost. The staff asked that the consultant conduct a detailed evaluation of the present plant. At the same time, the consultant conducted a financial analysis and review of the existing and proposed systems to develop negotiating strategies.

Seven months later, the council members were in a position to discuss the consultant's evaluations and to determine whether or not they could proceed to negotiate or open the process for competitive bidding. The consultant basically approved Cox's proposal for a 54-channel interactive system and concluded that the company had maintained its system well and had followed good management and local construction practices. Based on this favorable evaluation, the city decided to proceed with negotiations with Cox, reserving the right to reconsider if the negotiations proved unsuccessful.

Throughout the spring of 1981, two city officials met with representatives of Cox twice a week to rewrite the cable television ordinance. The ordinance they agreed on incorporates rate reviews, a community programming requirement, penalties for noncompliance, privacy protections, periodic performance and technical reviews, line extension requirements, and other state-of-the-art ordinance provisions.

On May 1, 1981, the city received Cox's formal proposal. This proposal was rejected, and Cox submitted another proposal on June 1. That proposal offered three tiers of programming, six premium pay services, and interactive and security services. In final negotiations, the company agreed to a "life-line" rate for the first tier for low-income senior citizen subscribers. By mid-June, the total package, including an in-depth staff report and draft ordinance, was submitted to the council for review and for a public hearing on the award of a license.

As the city was winding up its negotiations with Cox, a new local company, South Coast Community Cable Company (SCCC), was formed with the sole purpose of getting the cable television license away from Cox. This new company, which proposed service options at least comparable to those offered by Cox and at a lower rate, wanted an exclusive license to

Exhibit 9-1
Comparative Information on Renegotiations in Three Cities

City	**Austin** (90,000 subs) **Texas**	**Portsmouth** (15,500 subs) **Ohio**	**Santa Barbara** (68,500 subs) **California**
Penetration	57%	88%	80%
Original Operator	Capital Cable (Midwest Video, LBJ Corp.)	TelePrompTer	Cox
Competitive Bids?	No	No	No
New Owner?	American Television Corp.	No	No
Old System Capacity	12 channels	(12 activated)	12 channels
New Capacity	54-channel (dual) Text and Interactive	52-channel Text and Interactive	54-channel Text and Interactive
Franchise Expiration Date	1983	1981 (granted short extension)	1982
Began Renegotiation	1979	1980	1979
Completed Renegotiation	1981	1982	1981
New Basic Service and Rates after Upgrade	Tier 1 / 10 ch / $4.95 2 / 35 ch / $9.20 3 / 47 ch / $10.20 4 / 54 ch + T&I / $12.95	1 / 12 ch / $6.75 2 / 26 ch / $8.70 3 / 48 ch / $9.95 4 / 52 ch + T&I / $12.95	1 / 19 ch / $7.25 2 / 35 ch / $9.25 3 / 54 ch + T&I / $10.75
Pay Services Options by Tier	1 4 4 8	0 3 5 5	6 6 6
Period of Phased Upgrade	5 years: Channels — Period 12 to 23 in 18 months 23 to 36 in 4.5 years 36 to 54 in 5 years	18 months: Channels — Period 20 to 36 in immediate 36 to 52 in 18 months Interactive in 24 months	4 years: Channels — Period 12 to 19 in 4 months 19 to 35 in 5 months 35 to 54 by December 1985

T&I = Text and Interactive Services

operate in Santa Barbara.

This new company, composed of many influential Santa Barbara citizens, was able to exert tremendous pressure on the council to give an exclusive franchise to "a local company." Moreover, at the eleventh hour, SCCC proposed to significantly "lowball" Cox's already publicly proposed basic rates. Although there was great pressure on the council to consider SCCC's proposal, it decided to continue the renegotiation process with Cox. SCCC eventually withdrew.

Finally, on September 1, 1981, the council adopted the cable ordinance and two weeks later adopted a separate ordinance awarding a 15-year license to Cox Cable. In retrospect, city staff noted that informing the council and educating the community were the two most important elements of keeping the process moving ahead smoothly. According to the staff, there were times that council members, although they did not speak up, were apparently confused about why certain actions should be taken. They suggested that regular press releases from the city published during the negotiations might be helpful in educating the community.

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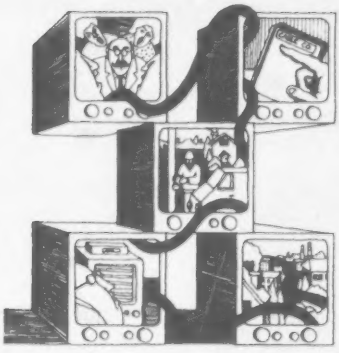

Noncommercial Access To Cable

By

Nancy J. Jesuale

Chapter 10: Noncommercial Access to Cable

In 1972, the Federal Communications Commission (FCC) first promulgated access rules for cable systems, requiring every system with 3,500 subscribers or more to set aside at least one channel for public, government, educational, and leased access to the system. Equipment, facilities, and channel time were to be made available to local users for a "reasonable rate." This rule was struck down in 1979 by the Supreme Court in the case known as *Midwest Video II*. The philosophy of noncommercial access to cable systems has gained wide acceptance, however, and hundreds of communities across the country have required that access channels and facilities be made available in local ordinances.

The actual development and forms of access programming are discussed in detail in volume I of this handbook. This chapter will elaborate on the philosophy of public access to the cable system and present some policy alternatives.

The Supreme Court has held that the First Amendment right of free speech includes the right to receive information from "diverse and antagonistic sources." Inherent in this principle is the recognition that a democracy must not suppress controversial opinions and that all citizens must have opportunities for self-expression. Freedom of the press to publish and editorialize is protected by the First Amendment. Broadcasting, however, uses the radio spectrum, considered to be a scarce, publicly owned resource. Thus, broadcasters are required to present discussion of controversial issues and conflicting viewpoints and to allow reasonable access to others to present their points of view over the air.

As broadcasting networks and publishing chains grew, so did the realization that sources of news and information delivery have been increasingly centralized. In an effort to limit concentration of ownership among media, the FCC has restrained broadcasting networks from owning more than seven broadcast outlets and from owning more than one outlet per television market. Moreover, cross-ownership of media is restricted to prevent concentration in each community.

Cable does not use the scarce radio spectrum for information delivery. It is similar to print in that there are no technological limitations on how many channels or "pages" of information can be presented. This very abundance of channels, however, was the impetus to require that cable systems reserve a portion of capacity to be controlled not by the owners but by the public. The concept of public access to cable was meant to insure that diverse voices had an outlet for self-expression in what was expected to become a ubiquitous community medium.

As the FCC first defined public access, it was to be available on a first-come, first-served, nondiscriminatory basis. Charges for channel time and television production facilities were to be set so that they were not prohibitive and did not accrue profit to the system owner. The concept of

public access to cable went far beyond what was required of broadcast television. Access was not to be limited to brief rebuttals or public service announcements; it was to be available in quantity, and program content was to be user controlled. Government and educational access was meant to allow public service institutions to use cable transmission as well. Cable was thought to be a medium that would enable more and more types of information and services to be delivered electronically, thereby increasing the quality of life in a community.

As discussed in chapter 1, the cable industry has challenged the interpretation of the First Amendment that would require it to provide access to the system, and the issue of access to cable systems may well end up in the Supreme Court again. However, franchising authorities have increasingly supported of the concept of access. Because most local governments issue only one franchise, certain service requirements have been prerequisite to the award of cable television franchises. Access has been a major local interest since the Federal requirements were removed.

Beyond minimal requirements imposed by the ordinance, access has become a "bid item" in most franchise awards. In most newer franchises, the local government's access requirements have been significantly exceeded by applicants anxious to win the franchise. These bids become binding under a contractual agreement. Once access channels and facilities have been promised by a cable operator, however, the policy questions become immediate. In most newer franchises, substantial channel capacity, funds for access operations, and expensive facilities have been promised. The local government, as party to the contract promising access to the cable, faces difficult problems in overseeing the fair allocation of these resources.

Access Policies and Local Government Involvement

Allocating the Resource

Some franchise authorities have required that access to the system be available but have not stipulated policies for using the resource. Others have required that access policies be included in the franchise application, and still others have set the policies independently from the operator. One basic question here is, who should control access channels and resources? In some cases, the city or an access advisory board appointed by city officials controls public, educational, and government access. In others, the company maintains control. A third option is an independent, nonprofit, community-based organization that controls access.

When the city controls access facilities and channels—whether all channels or simply the government channel—concerns about censorship and political manipulation must be considered. Most local governments have attempted some separation of access from government by appointing an autonomous advisory committee or city agency to set policies for channel use, allocation of funds, community programming standards, and arbitration of disputes among users.

When the cable company maintains control over access, it can be difficult to separate the company's profit orientation from its commitment to community programming. The company has the added pressures of dealing with user disputes, obscenity standards, and other controversies, while trying to meet both its commitment to access and its need to maximize subscribership.

Most communities prefer to form a separate nonprofit organization to facilitate access. Such a structure acts as a buffer zone between the company and the local government regulator and is designed to represent community interests and carry out the terms of the franchise agreement concerning access. Rather than being an access user itself, this group facilitates the efforts of other programmers to gain access to funds, facilities, and channel space.

Whichever model is put in place, the controlling entity will have to

- Allocate space on the channel(s);
- Allocate facilities;
- Develop and manage funding sources and revenues;
- Provide a forum for public input into policy;
- Insure that training and technical assistance is available to all sectors of the community; and
- Initiate public education and outreach to insure use of the resources committed.

These activities become more complicated in newly franchised major markets where significant funding has been committed by the cable operator (often millions of dollars over 15 years), and where some institutions and organizations have been singled out to receive direct access support while others have not. Political pressures on the city can be strong during and immediately after the franchising process as community organizations position to receive the most favorable access support. Often the franchise agreement stipulates that access funding from the company and from the city's franchise fees will be allocated by the local government. Unless there are clear criteria for distributing the funds and an access authority to implement the criteria, the local government may face an intense lobbying campaign from organizations wishing to receive funding. It can be difficult, under such circumstances, to guarantee "nondiscriminatory" access. Unless the local government implements or encourages a structure with equitable procedures for facilitating access to the system, it may invite direct confrontation from individuals and organizations that feel they have been treated unfairly.

If access channels are broken down into specialty channels for educational, government, minority, handicapped, neighborhood, foreign language, and other users, two potential policy problems arise. The first is the need to decide how to allocate limited funds and channels equitably among these identified user groups. The second is the need to define who shall be designated as the user organization to control the dedicated

resources. Some communities designate such specialty channels and funds to coalitions of interest groups to avoid closing off opportunities to "unrecognized groups." These coalitions should have a membership structure to allow new interest groups to participate in using the dedicated access resources.

Moreover, an appeals and monitoring structure is needed to insure fair allocation of resources. Often a membership organization performs this function. Unless this group is recognized by the local government, however, its effectiveness can be severely curtailed. This organization should be open to membership from all user groups and representative subscribers to insure that new users can have a voice and gain access to funds and facilities.

Assuring Efficient Use

Historically, access has been underfunded and underequipped, conditions that have led to its underutilization. In many new franchises, however, the cable operator's commitment to provide funds and facilities has been generous as a result of the competitive bidding process and effective community support of access. Whereas older franchises reserved only one channel for all access use or only shared channel space for access, in new franchises companies have often committed from 5 to 30 channels for various access uses as well as funding and staffing to support their use.

Access programming depends on public awareness and motivation to use the resource as well as an efficient structure to govern its use. Training in production techniques and equipment use must be readily available and affordable, and an effective community outreach program must be instituted or else the access channels may sit idle. This problem can be exacerbated when multiple channels are proposed to be controlled by specific groups and to be programmed with specific types of material. A tremendous investment of time and energy as well as funds must be made in access programming. Groups that have exclusive control of a channel may find that it will take them several years to generate enough programming to fill the time. In the meantime, if several dedicated access channels and studios sit idle, the cable operator may wish to reclaim them for commercial use.

To avoid underutilization of expensive access resources, some communities are exploring planned or phased implementation of access. The level of funding, equipment, channels, and staffing to be committed is determined by an ongoing needs assessment process. This process helps to prevent inefficient and expensive allocation of funds, facilities, and channels before they are operational. A needs assessment also documents commitment from potential access users that can be monitored. If their usage projections have been overly ambitious, channel allocations and other resources can be reallocated.

Disputes and Censorship

The underlying premise of access is that diverse and antagonistic sources shall have equal opportunity to present their views. Implementing

such a policy, however, can be difficult.

When the local government controls access, political pressure can be brought to bear to suppress certain viewpoints. When the cable operator controls access, economic pressure can be brought to bear. An independent community group will also feel pressure during controversial times. Thus, whatever the structure, a clear set of guidelines for allocation of funds, resources, and channel space must be published, adhered to, and subjected to public scrutiny and monitoring. Moreover, an appeals process for user complaints should be established. These guidelines should permit any user equal access to the resource. If access has been allocated separately to user groups, the responsible organization should be required to allow outside users to have access to funds and facilities provided by subscriber fees.

One difficult policy issue for local governments has been censorship on access channels. If any person can use a channel for any noncommercial purpose, the question of responsibility for obscene or slanderous programming must be addressed. Local operating policies can be established to prevent obscene and slanderous programming from being supported by funds provided to the authority. These policies should specifically state the criteria that must be met to receive funds, and these criteria should be applied uniformly to all users.

Keeping a program off the cable is another matter. The local cable operator can be held legally liable for slanderous or obscene programming that is cablecast over its system. Regarding access programming, however, many believe that the program producer should be held liable. A program cannot be censored prior to its production or cablecasting; therefore, the question of liability becomes critical. Many communities require access users to sign a liability form that places responsibility for all legal or economic damages experienced by the operator, as a result of cablecasting the program, with the program producer.

Summary

The policy context for access goes far beyond whether or not the cable operator should be required to provide access to the cable system. The manner and extent of both the operator's and the local government's involvement in access are important policy issues. Local governments that have incorporated extensive access requirements into their contracts with cable operators must realize that their policies on access will be important factors in deciding whether those commitments can be met. Moreover, the most critical elements for success in access are community participation and support and a fair and equitable structure for access users.

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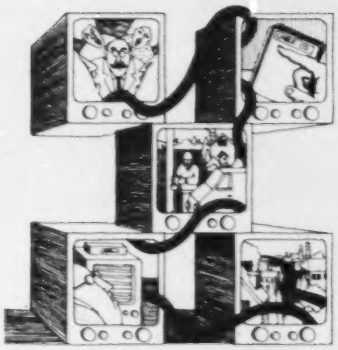


Leased Access To Cable

By
Howard J. Gan

Chapter 11: Leased Access to Cable

Much of the public policy debate concerning "access" to cable television systems has centered on noncommercial, community-oriented uses of cable channels. Increasingly, however, policymakers are focusing on the issue of whether cable systems should be required to provide access to leased channels for commercial, profit-making use by persons other than the system operator.

As advanced technology, high-channel capacity cable systems proliferate throughout the country, new markets are opening up for telecommunications services. Many businesses view cable systems as the most efficient and cost-effective method for distributing a wide array of entertainment, information, and other services to homes and businesses. However, businesses that may wish to use cable systems are by no means assured of obtaining access to cable channels for commercial use so long as the system operator retains full authority to determine the availability of channels.

Although Federal Communications Commission (FCC) rules formerly required cable systems to lease channels on a nondiscriminatory basis, such requirements no longer exist. This situation contrasts with common carrier regulations applied to telephone companies, which must let anyone willing to pay an established rate use their lines. Cable operators claim the legal right and the economic need to exert exclusive control over the use of their systems—particularly for commercial purposes—and to determine whether or not channels will be leased and at what rates. They also assert their need to control the content of the channels.

Business leaders and policymakers are concerned that the cable industry's asserted right to retain control over channel content places too much media and electronic information control in the hands of a single company. Some believe that mandatory provision of leased channels offers the best method for limiting anticompetitive activity by a cable operator; such provision would insure that businesses not directly affiliated with the cable operator would be able to use the system at a reasonable cost and compete directly with the cable operator's own services or offer additional services.

The potential for anticompetitive practices by cable operators is a function of a combination of factors. The first factor is cable's de facto monopoly status. Although cable franchises are generally nonexclusive grants of authority, the capital-intensive nature of a cable distribution system combined with other economic considerations normally results in only one cable system serving a geographic area. Thus, there is no direct competition among cable systems. Usually, a cable operator will not allow competing or alternative cable services to use the one system available to reach consumers or businesses.

The second factor is a cable industry trend toward extensive concen-

tration of control by a few vertically integrated media corporations that produce and distribute pay program services over cable systems they own.

A single profit-maximizing business that retains full control of all channels and programming has a natural incentive to restrict or prevent competitors' access to its systems to avoid price competition and market share reductions. The issue is whether it is appropriate to require cable operators to provide leased channels to insure that entities other than the system owner have access to and can use the cable system for commercial purposes.

Underlying Principles: Freedom of Speech and Economic Competition

The concept of leased channels is important for two reasons. Leased channels may encourage economic competition. They may also protect basic First Amendment interests within the community. The First Amendment to the Constitution protects the freedom of speech and the free flow of information within a community.

Justice Hugo Black stated in the case of *Associated Press* v. *The United States:*

> [The First Amendment] rests on the assumption that the widest possible dissemination of information from diverse and antagonistic sources is essential to the welfare of the public. . . . [F]reedom to publish means freedom for all and not some. . . . [F]reedom of the press from government interference under the First Amendment does not sanction repression of that freedom by private interests.

Justice Felix Frankfurter's concurring opinion in that case stated that a company engaged in the distribution of news and information "has a relation to the public interest unlike that of any other enterprise or pursuit for profit." The public interest in the free flow of information "may be defeated by private restraints no less than by public censorship."

To the extent that a cable operator has total control over all of the channels on the system, he has the ability to restrict the flow of information within the community. Moreover, if the cable operator can prevent other businesses from using the cable system, and alternative methods of distribution are not available at comparable costs, the operator has the ability to restrict economic competition. The fundamental question is one of control. Should the cable operator, as the system's "gatekeeper," select what may appear on every channel on a system? Or should some cable channels be set aside for use by others?

Telephone companies and other telecommunications common carriers merely provide the transmission system to carry messages; a carrier cannot control the content of those messages. At the other extreme, newspapers have total control of the content of their publications, limited only by laws applicable to libel and obscenity. Broadcasters also exert con-

tent control but, as public trustees, affirmative obligations and restrictions are imposed on the manner in which they may operate.

Regulatory Jurisdiction

When the FCC adopted comprehensive rules and policies for cable television in 1972, it sought to encourage cable to develop its full potential by providing broadcast-type local origination programming and common-carrier-type "access" functions. In addition to requiring noncommercial public, educational, and government access channels, the FCC required that channel capacity be made available for lease, on a first-come, first-served, nondiscriminatory basis.[1] Systems were also required to add channel capacity as needed to accommodate demand for additional leased channels.

In 1979, the Supreme Court ruled that the FCC could not mandate the provision of "access" channels (including "leased access") because such rules amounted to an imposition of "common carrier" regulation of cable.[2] Because the FCC chose to regulate cable pursuant to its authority over broadcasting, the Court ruled that the Communications Act did not permit regulation of cable as both a broadcaster and a common carrier. As a result, all FCC access requirements were struck down. The power of State and local governments to require provision of access channels, however, was not affected by this ruling.

In the case of *NARUC* v. *FCC*, 533 F. 2d 36 (1976), the U.S. Court of Appeals struck down the FCC's attempt to preempt State or local authority over certain *nonvideo* services. The *NARUC II* decision, as it is called, permits States to regulate rates and terms for provision of intrastate, nonvideo services.

The Cable Industry's Position on Leased Channels

The cable industry argues that cable TV systems are "telepublishers," entitled to the same rights under the First Amendment as newspapers and other print media. If this position is upheld by legislation or court decisions, cable systems, like newspapers, could not be required to lease part of their channel capacity to third parties. Industry representatives also suggest it is too soon in the evolution of cable technology and services to mandate the provision of leased channels because it has not been shown that competitive alternatives to cable are unavailable.

The cable industry believes that any decision as to who may use cable channels and under what conditions should remain with the cable operator, with rates as well as program content subject exclusively to the system operator's discretion. It holds that the individual system operator should be free to negotiate whatever agreements he wishes with potential users of

[1] "Access" to the cable systems provided for four distinct categories of use: public, educational, government, and leased.

[2] See *FCC* v. *Midwest Video*, 440 U.S. 689 (1979).

channels, or not to enter into any agreements at all. In addition, the industry argues that cable services must be sold to consumers as a package, requiring the operator retain the discretionary power to determine the proper mix of services and to avoid a concentration of certain types of service. For example, several different companies might wish to lease channels to provide local real estate listings or local news. If operators are required to lease channels to all comers on a nondiscriminatory basis, service variety might be lessened, resulting in reductions in both subscribership and overall system revenues.

The industry vigorously challenges assertions that cable is a true monopoly, since a variety of other communications media compete against cable for the consumers' attention, including TV broadcast stations, multipoint distribution systems, subscription television stations, video cassettes, video discs, and—at least for the provision of teletext, security, and data services—the telephone company. In any event, the industry argues, the government need not mandate leased channels because potential users of the system may sue under the antitrust laws if they are denied use of a facility deemed essential for them to carry on their business.

Cable companies are also concerned that leasing channels to service providers that may compete with the cable company itself for subscriber revenues (such as movie channels) may threaten the system's economic viability. The rationale is that the leasing charges would not be sufficient to compensate for the reduction in revenues from the operator-provided service. The cable companies also claim serious technical problems could arise that might be difficult to overcome if leased channels were required services such as home security or data retrieval, for which sophisticated subscriber terminals and computer services are needed.

Perhaps the greatest concern of the industry is that leased channel requirements could precipitate partial common carrier regulation by State agencies immediately and could lead to comprehensive common carrier regulation in the future. In the *NARUC II* case, the U.S. Court of Appeals found that the FCC could not preempt State regulation of cable-leased channels for intrastate two-way nonvideo services. As a result, State public utility commissions can presently assert jurisdiction over certain leased channel services and might be tempted to impose common carrier regulations on other cable services. In the industry's view, this would add unnecessary levels of regulation that would inhibit cable's ability to compete in the marketplace and could stifle risky investments in new technology and services.

Response to the Industry Position

With regard to the industry's First Amendment claim of "telepublisher" status, at least one U.S. Court of Appeals decision (the *Boulder II* case) has held that any First Amendent analysis should take into account cable's de facto monopoly status, the government's role in granting

a franchise to use the public rights-of-way, and the public's interest in insuring diversity of information sources. That is, a cable operator's First Amendment rights may be subject to reasonable limitations, as is true of broadcasters, due to cable's unique attributes.

The economics of the marketplace for telecommunications services are an important element in any policy decision. Although cable does not have a total monopoly over distribution of video, audio, or data services, cable systems do have substantial and perhaps dominant market power in certain areas due to their ability to bundle together and cross-subsidize several different services. Furthermore, the increasing trend in the cable industry toward vertical and horizontal concentration may place the power to dominate markets in relatively few hands.

The industry is correct in arguing that the antitrust laws provide one remedy for unreasonable restraints of trade. Antitrust litigation, however, is not only complex and expensive to pursue, it may provide a cure after the patient is already dead. Government policymakers want to promote marketplace competition and insure diversity of information and services in the first instance. After-the-fact remedies may not be regarded as an adequate substitute for well-considered and forward-looking telecommunications policymaking.

Alternative Methods for Providing Commercial Access

Most communities that have franchised cable systems (including those in States where a State agency has regulatory authority) have no provisions in local franchise agreements or regulatory ordinances requiring the cable system operator to make channels available on a leased basis. Few local governments have addressed comprehensively the desirability or need for leased channel provisions. The added difficulty of resolving a variety of complex regulatory questions has further inhibited the development of such policies in local ordinances and franchise agreements.

In some communities, particularly those that have recently granted franchises, provisions require that the system operator make one or more channels available on a leased basis. In many other systems, the provision of leased channels is encouraged in the Request for Proposals (RFP), but is not mandated. Voluntary commitments by franchise applicants are then incorporated into binding contractual agreements.

Voluntary Commitments

Voluntary provision of leased channels may be imperfect, however, during this period of regulatory transition and technological evolution for the cable industry. But it is one method by which a local franchising authority can obtain binding agreements from a franchisee that a reasonable number of leased channels will be provided at fair rates. Voluntary, contractually binding commitments by cable companies to provide leased channels are a legally effective method of insuring that some leased

channels are provided. In such instances, the cable operator may retain substantial control over who can lease a channel and what programming or services will be provided. Rates for use of the channels are not generally regulated; however, there is ordinarily a general requirement that access must be provided at fair and reasonable rates. The local government may retain authority to oversee and investigate the franchisee's behavior and possibly impose more detailed regulation if abuses are found.

Mandatory Provisions

An alternative approach is to require a specific number or percentage of a cable system's channels to be set aside for leased purposes. Again, this approach leaves substantial discretion with the operator to select among potential lessees and to set rates on a case-by-case basis.

A mandatory leasing policy that does not impose rate regulation may be less subject to preemption by the State or the Federal Government and would entail limited oversight by local government officials. The operator would not be permitted to unreasonably deny leased service to potential users but could negotiate specific elements of the lease arrangement.

Because demand for leased channels is just now developing, it is difficult to determine a reasonable number of channels to set aside for leased purposes. Many variables must be considered, including the size of the community and the total system channel capacity. One approach is to obtain assurances from the system operator that at least one leased channel will be available initially, and that additional channels will be provided *upon request* by potential users up to an established ceiling.

Both the voluntary and general leased channel requirement approaches share a common problem. The system operator retains control over the selection of lessees and the rates charged. This does not solve the basic problem of potential anticompetitive actions by the operator either in discriminating against certain users or in pricing to freeze out competitors who might otherwise lease capacity on the system.

Several approaches have been developed to better assure nondiscriminatory access by lessees at reasonable rates. Boston, for example, gives control of a set number of leased channels to an independent board that negotiates terms and rates with potential lessees. Some cities require the cable company to provide additional leased channels upon demand, up to an established ceiling or up to the limit of unused channels on the system. In high-capacity cable systems, it may be advisable to obtain the operator's agreement that a minimum number or percentage of channels will be available for lease. The great differences among communities, however, in both total system capacity and the number of operator-used channels preclude any magic numerical rule of thumb. The goal should be to require enough channels so that the operator's vertically integrated services face real competition and to require enough channels to allow space for additional services that the operator does not offer.

Operators have tried to avoid common carrier status by establishing joint venture agreements with the lessees of channels. The operator and the service provider become partners, with joint interests in the venture. Sometimes the system operator and the partner will share in the investment costs of equipment (for example, the character generator for text news services, local origination equipment for broadcast type news, and equipment for security services).

A variety of arrangements exist for operator compensation for the use of leased channels. Some leases give the operator a predetermined percentage of total revenues from the service on the board leased channel. This arrangement is characteristic of channels in which advertising is the primary source of revenue. Some lease arrangements call for a flat fee negotiated on a per subscriber basis. Other arrangements combine both the percentage of revenues and per subscriber approaches. Absent regulation of the details of lease arrangements, market forces govern the terms and charges negotiated for the lease. Serious experiments with lease arrangements began in 1981. Lessees will, for a time, enjoy the economic advantage as operators seek them out to provide additional services to fill all the channels on the new large-capacity services. In time, this balance will shift as the new systems fill and operators begin to pick and choose among potential lessees based on those that will add most to the operator's profits.

Summary

Modern cable systems promise municipalities the potential of a new information network within the community. If this promise is realized, cities need to insure that all citizens will have reasonable access to the system and all information sources will have reasonable use of the system. Leased channels offer an important mechanism to achieve this goal.

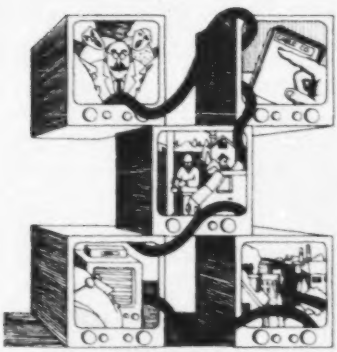
Local governments should avoid detailed regulation of leased channels wherever possible by simply requiring that leased channels be made available on a nondiscriminatory basis and at reasonable rates. Local governments should not get embroiled in potentially complex, day-to-day regulation of leased channels or the rates charged, except as a last resort. So long as a cable system has excess capacity and is willing to negotiate with potential lessees, local governments should not be overly concerned that the operator has unfair market power. Only when a pattern of exclusion or price discrimination develops should municipalities begin to consider stringent regulatory oversight.

Cable television systems may well become the dominant source of all information in our communities. Home entertainment, news, business information, and specialized telecommunications services should be widely available on cable systems in a few years. Competitive methods of obtaining television programming—DBS (direct braodcast satellites), STV (subscription televison), MDS (multipoint distribution service), traditional television broadcasting, video cassettes, and video discs will exist. However, these

program distribution methods are likely to supplement cable service, not substitute for it. Competing entertainment services simply will not be able to provide the wider variety of services a cable system can offer, with its large channel capacity and interactive capabilities.

If program suppliers or service providers wish to reach customers or businesses within the community, they may well be forced to use the cable system or fail. There may be no economically viable alternative for the local cable distribution of services. Thus, if the cable system operator controls *all* of the numerous video, audio, and data channels on his system, he may well have total control over competitive entry into the local communication marketplace. Local governments should therefore consider an appropriate but flexible mechanism for insuring that leased channels are made available.

12



Antitrust Issues In Cable

*By**
Howard J. Gan

*The author and editors gratefully acknowledge the contributions of John Mansell and Michael W. Evans (Associate, Preston, Thorgrimson, Ellis and Holman) to this chapter.

Chapter 12: Antitrust Issues in Cable

The Federal antitrust laws forbid anticompetitive activity. Many cable television franchising and regulatory activities might be interpreted, at least theoretically, as anticompetitive. For example, a local government decision to select one franchise applicant over others could be challenged as anticompetitive and a violation of the antitrust laws.

Until recently, many municipalities believed that regardless of the theoretical anticompetitiveness of their activities, they were immune from antitrust lawsuits under the "State action immunity" doctrine the Supreme Court fashioned more than 30 years ago. This belief has been undercut by a recent series of Supreme Court decisions culminating in the *City of Boulder* decision issued in January 1982. These decisions make clear that municipal cable activities (as well as many other municipal activities) *can* subject a municipality to antitrust lawsuits. Consequently, it is imperative that all municipalities involved in cable activities become familiar with the antitrust laws.

The *City of Boulder* Decision

The most recent and important decision regarding municipal immunity is the *City of Boulder* decision.[1]

The case involved the Community Communications Company (CCC), which in 1966 had obtained a 20-year nonexclusive franchise covering the entire city of Boulder, Colorado. Until 1979, however, CCC had "wired" only one area, covering approximately one-third of the city, in which over-the-air reception was inadequate. In 1979, CCC informed the city that it planned to wire the rest of the city and expand its programming. During the same time, another company informed the city that it was interested in obtaining a second franchise to serve the city. The city council, recognizing that companies almost never "overbuild" an existing cable system with another, considered adopting a construction moratorium so that it could fully consider its franchising options. CCC then accelerated its expansion. The city council responded by enacting a 90-day moratorium on CCC expansion in order to prevent CCC from wiring even more of the city and thereby impeding eventual competition.

CCC then filed suit in Federal district court seeking a preliminary injunction prohibiting the city from enforcing the moratorium; it charged the city with conspiring with the potential competitor company to restrain trade by preventing CCC from extending its service to new customers. The city answered that its acts were (a) a valid exercise of its "home rule" power to act in local matters, granted pursuant to the Colorado constitution; and (b) authorized by the State legislature, and therefore exempt from the antitrust laws under the "State action" doctrine.

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[1] *Community Communications Corp.* v. *City of Boulder*, 50 U.S.C. W. 4144 (Jan. 13, 1982).

After the district and appeals courts considered the issues (and came to different conclusions), the Supreme Court reviewed the case. In a 5-3 decision, it held that municipal action is not "State action," regardless of its characterization as a lawful exercise of home rule authority, unless it is pursuant to a "clearly articulated and affirmatively expressed" State policy to displace competition. More specifically, the opinion made the following points:

(1) In our "dual" system of government, only federal and state governments are sovereign; not municipal governments. Consequently, municipal actions are not entitled to the same federalist deference as state actions are.

(2) The "state action" exemption applies to municipalities only if their actions are furthering or implementing a "clearly articulated and affirmatively expressed" state policy.

(3) Home rule power may guarantee local autonomy but does not by itself constitute a clearly articulated and affirmatively expressed state policy.

What the Court did *not* say is almost as important as what it did say. The Court raised but left unresolved several important issues. One is whether, if municipal action is not immune, it nevertheless is analyzed according to a more lenient standard than private business action. Another is whether, if a municipality commits an antitrust violation, it is subject to lesser remedies than private businesses.[2]

After *City of Boulder*, municipalities attempting to minimize antitrust risk must address two basic questions regarding cable activities.

1. Does a State policy exist to displace competition that is sufficient to confer community?
2. If the existence of such a State policy is doubtful, is there a significant chance that the activity violates antitrust laws?

Immunity

Different States have taken different approaches to cable regulation and each approach raises different immunity questions. It is impossible here to review thoroughly all of these questions. Nevertheless, some preliminary observations can be made.

First, the Supreme Court apparently will not require a State statute to *expressly* establish a State policy to displace competition. This is because in *City of Boulder* the Court cited an earlier appeals court opinion that stated that a trial judge determining whether a particular activity is immune should evaluate "all evidence which might show the scope of legislative intent." Thus, it appears that in some circumstances a State policy to displace competition can be inferred.

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[2]A third question is whether municipal activity must be actively supervised by the State, as it has been held that private activity must be. In *City of Boulder*, the Supreme Court raised but left unanswered this issue.

Second, this evidentiary standard is flexible. It gives courts considerable leeway and makes it difficult to predict precisely what they will conclude about a particular statute.

Third, although States have taken different approaches, the approaches fall into three general categories for the purpose of immunity analysis.

1. Eleven States regulate cable in whole or part through a State agency.
2. Fifteen States have expressly given municipalities some authority to regulate cable.
3. Twenty-four States neither regulate cable through a State agency nor expressly give municipalities some authority to regulate cable.

Each category requires a slightly different immunity analysis.

The first category—States that regulate cable in whole or part through a State agency—has two subcategories. One subcategory includes States that regulate exclusively through a State agency and give no role to municipalities (e.g., Alaska); in these States, municipal immunity is irrelevant because no municipal action is allowed. The second subcategory includes States which share cable regulatory authority between the State and municipalities (e.g., Massachusetts, Minnesota, New York). In these States, the provisions establishing the municipal share of the regulatory authority must be analyzed closely to determine whether and to what degree they confer immunity. Generally, though, the existence of a statewide cable regulatory system in which municipalities play a critical role bolsters the argument for some degree of municipal immunity.

The language of the Massachusetts State cable statute, for example, does not contain an express statement of a State policy to restrict competition. However, the statute does provide that a municipality shall choose "*that applicant* or applicants" (emphasis added) it believes will best serve the public interest. This language might be interpreted as indicating the State has not only contemplated but affirmatively authorized a municipality to limit competition by selecting a single applicant if it wishes to do so. This interpretation is supported by the existence of State oversight of municipalities' actions; it reasonably could be inferred that the State legislature intended to give municipalities the authority to restrict competition, subject to the State's oversight. If such intent were found, immunity probably would exist.

The second category is States that have expressly given municipalities some authority to regulate cable. A typical statute in this category, however, does not contain an express statement of a State policy to displace competition. Consequently, whether immunity exists depends on the inferences that can be drawn from the framework of municipal regulation that the statute establishes.

The third category is States that neither regulate cable through a State agency nor expressly give municipalities authority to regulate cable. In

these States, the case for immunity is weakest. It is difficult to envision what a source of immunity might be. One possible source is a State statute governing general municipal franchising of public utilities (although the question of whether cable is a public utility arises).

Liability for Municipalities That Are Not Immune

If a municipality is not immune, the question becomes whether its activities violate the antitrust laws, not a question easily answered. The applicable antitrust laws are sections 1 and 2 of the Sherman Act. Section 1 prohibits concerted action in restraint of trade; section 2 prohibits monopolization or attempted monopolization.

Both sections ordinarily are applied according to a flexible standard, called the "rule-of-reason," which focuses on whether an activity promotes or suppresses competition. (In some circumstances, a section is applied according to a stricter "per se" standard, but several precedents indicate that this standard should not be applied to governmental activities.) This requires a case-by-case analysis that examines the actions taken, the relevant market, and other economic and competitive factors. For example, a decision to grant a single franchise might be upheld in one community and stricken in another. Because so many factors can be examined, in such a loose way, decisions will be somewhat ad hoc. This approach inhibits predictability and encourages extensive litigation.

Nevertheless, municipalities can act to protect themselves. First, they can minimize risk by developing a clear record establishing the legal, economic, and public interest justifications for their actions. Courts are likely to grant a substantial degree of latitude to local government decisions that are shown to be reasonable and well considered.

Second, municipalities should be especially wary when an existing franchise expires. New companies may seek franchises to overbuild or replace the existing system operator. At the same time, the existing company will seek to protect its investment and prevent the city from replacing it with another company. Thus, either the existing operator or new applicants may pose an antitrust threat when the city negotiates only with the existing cable company and refuses to consider new applicants, or when the city seeks to replace the existing company with a new company at the end of the franchise term, allowing the existing franchise to expire.

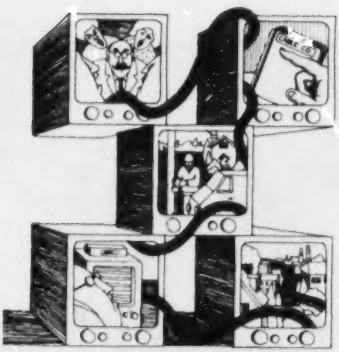
Third, municipalities granting single, nonexclusive franchises may be able to justify such action, as a reasonable restraint of trade and a legitimate exercise of local regulatory authority, based upon a number of considerations. The first is the municipality's traditional "police" power to protect the public health, safety, and welfare. Protection against such practices as having several different companies digging up the streets, installing multiple wires and electronic equipment on poles, as well as other hazardous, disruptive or unsightly practices are considered legitimate municipal concerns. In addition, there are legal and policy precedents to support selective or discre-

tionary municipal licensing and procurement practices which are based on a fair and competitive application process.

Summary

The *City of Boulder* decision has created considerable uncertainty. It will be several years before enough lower court decisions have been decided for a clear map of the boundaries of antitrust exposure to emerge. Until it does, the wise course for municipalities is to proceed cautiously, with the advice of counsel, whenever considering cable activities which might be interpreted as anticompetitive.

13



Consumer Issues In Cable

By

Bruce Jacobs

Chapter 13: Consumer Issues in Cable

As cable grows and offers new services, such as home banking, home security, home shopping, opinion polling, and energy load management, its use will raise an increasing number of consumer issues. Some of the issues that local governments may want to address are the processing of customer service complaints, deceptive advertising and fraudulent direct marketing, sales practices of the cable operators, the possible subscriber purchase of equipment, universal service, offensive programming, and individual privacy. Consumers themselves may want to deal directly with cable operators to solve some of these problems. Several options consumers may wish to pursue to present their complaints more effectively are discussed at the end of this chapter.

Customer Complaints

Informal discussions with municipal officials recently indicated that the volume of complaints is not large and that cable companies are usually fairly responsive to government attempts to mediate problems. For instance, a cable official in Seattle, Washington, reported an average of two complaints a day for a system serving 50,000 homes. Typically, consumers are concerned about delays in scheduled installation of service, billing errors, and refunds necessitated by interruptions in service. In some cases, the reason behind a complaint is that the subscriber's television is malfunctioning, not the cable system.

The municipal officials surveyed agreed that they can best assure operator compliance with complaint procedures and other ordinance provisions when they have (a) a well-drafted franchise ordinance and agreement and (b) the authority to regulate rates. The first defines the rights and responsibilities of the parties. The second, according to municipal officials, is often necessary to get the operator's cooperation in dealing with issues that are covered inadequately or omitted in the ordinance or agreement.

Many of the recommended franchise and ordinance provisions are discussed in chapters 3 and 4. These provisions should include the establishment of a procedure whereby subscribers can notify the operator of problems; for example, a telephone line for complaints. The cable company should also be required to respond to complaints within a specified time. Provisions that mandate a partial refund to the subscriber if service is not restored within a certain time may protect subscribers further. By requiring a top operating officer of the cable company to attend local public meetings, local officials may also be able to assure the operator's continued attention to complaints.

Complaints may also be minimized if the operator is required to distribute materials to new subscribers that explain common technical problems that may arise and that clearly explain the operator's billing system, including any advance billing practices. Some officials have suggested re-

quiring the operator to give all new subscribers a copy of the sections in the ordinance and agreement that describe consumers' rights and complaint procedures.

Advertising

Advertising currently provides less than five percent of the revenue of the typical cable system, but that percentage is expected to increase significantly in the coming years. As new advertiser-supported cable programming networks develop and more people begin to watch cable programs, local and national advertisers can be expected to buy more time on cable. Advertisers will also be attracted by the greater freedom currently offered by cable. Cable advertisers are experimenting with longer ads, greater direct involvement in program production, and different formats (including for example, advertising in the form of talk shows that discuss the advertiser's product). Some consumer advocates have raised questions about the impact on public opinion of large advertising budgets as well as potentially deceptive formats of advertiser-sponsored programming.

Current restrictions on cable advertising are minimal. Although Federal regulation of broadcasters requires television and radio licensees to make reasonable efforts to eliminate false, misleading, and deceptive ads, cable operators have no such legal responsibility. Cable operators, like broadcasters, are required to indicate clearly the sponsorship of an ad, but this requirement applies only to what the Federal Communications Commission (FCC) calls "origination cablecasting"—that is, programming under the operator's control. It is not clear whether this rule covers cable network programming.

The cable industry is working on a program of self-regulation of advertising. For years, the National Association of Broadcasters has promoted a rather detailed advertising code that, among other things, requires broadcasters to reject ads when their truthfulness is suspect and to exercise greater care in accepting ads that involve direct sales to the public. In addition, the three major television networks and most local stations prescreen their advertising to insure adherence to minimum standards. In October 1980, the National Cable Television Association established an advertising committee, which plans to issue advertising guidelines for cable operators by mid-1982.

Advertising codes can also be used to increase ad revenues. The NAB Code, among other things, prevented advertisers from displaying more than one product in any one commercial. Because of this and other provisions, the Justice Department successfully challenged the code, and the NAB may soon drop it altogether.

In the absence of industry self-regulation, local franchise agreements could require that individual cable operators prescreen advertising that they sell and make a reasonable effort to keep deceptive ads from being televised. Other issues, such as whether certain formats are deceptive, may be

addressed in more broad-ranging inquiries by the Federal Trade Commission. In the meantime, the cable industry can be encouraged to continue working on a code of advertising practices that would require both the national cable networks and the local cable operator to prescreen advertising.

Direct Marketing

In the future, industry observers expect expansion of the use of cable for the direct marketing of goods and services. This marketing may be of the traditional broadcast variety, in which a product is advertised and the viewer or listener is urged to call or mail in an order, or, when possible, to use a system's interactive capability by pressing a button to register an order for an advertised item. One problem with purchases of this sort is that the customer cannot examine the merchandise or ask questions of the seller prior to placing an order. Another problem, particularly for purchases made through an interactive system, is that they may be based on impulses that are later regretted.

There is currently some Federal regulation of door-to-door and mail-order solicitation. For instance, customers ordering goods from a door-to-door salesperson have a "cooling off" period of three days in which to cancel an order. Goods ordered through the mail must be delivered within 30 days. These regulations, however, do not apply to direct sales over broadcast or cable television.

Although it is generally conceded that the most effective way to prevent unscrupulous direct marketing over cable would be through Federal regulation, local governments can also take some steps. For instance, franchise agreements could include provisions requiring that purchases made through the cable system be subject to a "cooling off" period similar to the door-to-door solicitation regulations. Local governments could also require that cable operators make available to customers the addresses of the corporate headquarters of any companies that use the cable system for direct marketing. Typically, these companies give only post office box addresses or use telephone answering services, both of which make it difficult for customers to register complaints. Local governments might require the cable operator to insist that merchants advertising on the system set up a procedure for handling customer complaints and perhaps require the marketer to offer a warranty for its product as a condition for buying advertising time.

One Federal official has suggested that it may be reasonable to place more stringent restrictions on cable operators than on broadcasters because the revenues they receive from advertising are sometimes directly tied to the volume of an advertiser's sales. Broadcasters generally charge a flat fee for advertisements. Cable operators, however, have more difficulty in accurately measuring the size of their audiences and, instead of charging a flat fee, often take a share of the marketer's revenues; in effect, they enter into a partnership with the advertiser.

Sales and Advertising Practices of the Cable Operator

Some communities have had trouble with the advertising and sales practices of the cable operator. Some cable operators, anxious to sell their service to as many customers at as high a rate as possible, have given potential customers incomplete price information, failed to provide information about low-cost items, and used other questionable selling techniques.[1]

Local officials can take several steps to limit deceptive sales practices. They can include in the cable ordinance or franchise agreement a requirement that the operator provide each potential subscriber with a complete list of package options and prices. Local officials also could require all literature sent to potential customers and all standard telephone and door-to-door sales presentations made by the company's employees to be screened for accuracy and truthfulness by the local government's franchise administrator.

Subscriber Purchase of Equipment

At present, most consumers lease the equipment, such as set-top converters, associated with their cable subscription. So far, consumers have been generally content with this rental arrangement, probably because the equipment tends to wear out rapidly and needs repair frequently. In addition, the current absence of national intersystem standardization and readily available purchasing alternatives has made subscriber ownership of equipment almost impossible.

Over the course of a 15-year franchise, however, this situation could change. As has happened with telephones, purchasing equipment may become a more economical alternative and may provide competitive options not offered by the cable operator. "Cable ready" televisions, which may eliminate a basic subscriber's need for a converter, are one example of the development of such options. Cable operators and local officials will have to decide whether to allow subscribers to own and install their own equipment, whether the operator should sell as well as lease equipment, and what compatibility restrictions should be placed on any non-operator-supplied equipment connected to the cable system. To deal with this issue in the future, officials may need to include provisions in the cable ordinance or franchise agreement that address the "lease versus sale" question and that establish compatibility standards.

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[1]One operator in Minnesota sent sales material to existing subscribers informing them of more expensive packages of programming and requiring the customers to return a coupon if they did *not* want the advertised packages. Another operator, using stationery that indicated the sender was a research institute, sent potential subscribers a packet of materials requesting their participation in a study that required the participants to subscribe to cable service. The operator found that this method of marketing its cable service was effective not only in getting people to subscribe but also in retaining them as subscribers. The participants presumably believed that they would adversely affect the study's validity if they dropped out. Apparently, the cable operator had no intention of ever using the questionnaires filled out periodically by the subscriber/participants; the entire effort was intended only to boost and maintain sales.

Universal Service

Some cable operators and local officials have attempted to address this complex issue of an "information gap" by promoting the idea of a "universal service" tier on the cable system, which would offer limited cable services for no monthly fee.

Local officials are increasingly concerned that persons unable or unwilling to pay for cable service will be excluded from certain public information and services available over cable, and that restricting information to those who pay will widen the growing information gap between rich and poor. The problem becomes more serious as municipalities contemplate offering direct health and social services, job listings, and public hearings over cable and as transactional and polling services become available to cable subscribers.

Most universal service proposals are designed so that the tier does not require a converter. Also, an installation fee is charged to avoid subsidy by the paying subscribers of the nonpaying subscribers. A minimal package of programming is usually available, including public, municipal, educational access channels, certain community data channels, and local broadcast reception.

Offensive Programming

One of the most explosive issues local officials may have to deal with is offensive programming. Cable's abundance of channels is likely to include sexually explicit programming as well as controversial material.

Long-established First Amendment principles apply to cable as to other media. Local governments cannot engage in prior censorship of cable programming, but they can forbid obscenity. The Supreme Court has held that obscenity is not protected by the First Amendment. The FCC currently prohibits cable operators from televising obscene or indecent programming, but that restriction applies only to programming within the control of the operator, a category which may or may not include most satellite-delivered programming and which probably does not include access programming. This leaves open for State or local legislation the issue of obscene programming that is not operator-controlled.[2]

In *FCC v. Pacifica Foundation,* 438 U.S. 726 (1978), the Supreme Court upheld the FCC's right to restrict broadcasting of indecent speech, largely because of the intrusive nature of broadcasting. The FCC was permitted to decide that speech that was not obscene but nonetheless objectionable or "profane" could not be aired at a time when children were likely

[2]The Supreme Court has established a three-part test for assessing the constitutionality of legislation or regulations governing obscenity. In *Miller v. California,* 378 U.S. 577 (1964), the Court said that such legislation is constitutional if it takes into account (a) whether the average person, applying contemporary community standards, would find that the work, taken as a whole, appeals to the prurient interest; (b) whether the work depicts or describes, in a patently offensive way, sexual conduct specifically defined by the applicable State laws; and (c) whether the work, taken as a whole, lacks serious literary, artistic, political, or scientific value.

to be in the audience. The FCC has never tested the *Pacifica* ruling's applicability to cable, and the constitutionality of existing FCC regulations prohibiting indecent programming over cable remains undecided.

As discussed in chapter 1, the National Cable Television Association (NCTA) argues that cable is different from broadcasting in important respects and that therefore cable operators should be given greater freedom from content restrictions than might be appropriate for over-the-air television or radio. NCTA notes that cable enters a home only if the adult residents choose to subscribe to cable service and that adult programming is generally limited to pay tiers that the subscriber must specifically request. NCTA also argues that cable differs from broadcasting in that program guides offered by cable operators generally provide more advance information to subscribers about potentially objectionable programming. NCTA also points out that lock boxes can be provided for subscribers who want to block out specific programming to prevent unattended children from watching.

Some analysts believe that NCTA's view does not adequately consider the possibility that objectionable broadcasts may be made available on a basic tier of programming. These channels enter every cable subscriber's home, even if they subscribe only for better broadcast TV reception. Although program guides and lock boxes can be valuable aids to program selection and parental guidance, they may not always provide adequate safeguards. Consequently, some observers suggest that the courts may be willing to accept limited restrictions on indecent programming, at least on the basic tier. Possible restrictions could involve the obligation of the operator to preview programming and screen out shows that violate some lesser standard than "obscenity."

The answers to these questions are less clear when we look at restrictions imposed by cable operators themselves. The basic principle here is that the First Amendment prohibits only government censorship. The First Amendment does not prohibit private actions such as decisions of a newspaper editor to delete a particular story or refuse an advertisement. Someone whose programming is kept off a cable system, however, might argue that the cable operator's restrictions, to the extent that they were imposed by the franchising authority during the franchising process, are indirectly the restrictions of the local government and, as such, impermissible censorship.

To the extent that the franchisee operates through a government-issued franchise award, some would argue that the operator should be seen as an agent of the government at least for the purposes of limiting its right to select from among programmers. According to this "State action" view, the operator might have to serve as something of a common carrier, establishing impartial standards by which it would select programming.

The same argument might be applied, perhaps even more logically, to channels run by a nonprofit access center, particularly when the center is established, and its board of directors is appointed, by the local govern-

ment. A 1981 U.S. court of appeals decision, however, upheld the right of a State-owned public broadcasting station to refuse to air the controversial program "Death of a Princess," thus weakening this "State action" line of reasoning.

Local governments can help avoid problems with objectionable programming by requiring operators to provide a detailed program guide if they do not already offer one. The ordinance or franchise agreement can also require that lock boxes be made available for a reasonable charge to any subscriber upon request.

Individual Privacy

The development of large, multiservice, interactive cable systems has brought with it an increasing concern about the potential for violations of individual privacy. To the extent that cable systems will be used not only to view home entertainment programming, but also to do home banking and shopping; to place airline and dinner reservations; to conduct opinion polling; to gain access to electronic libraries, data banks, and newspapers; and to provide security services, they will be a potential source of vast centralized records of personal information. For instance, cable security systems alone may permit monitoring of an individual's comings and goings and may allow computer storage of detailed home blueprints for the local fire department or of personal medical information for emergency rescue personnel.

The accumulation of all this personal information could raise threats to personal privacy. Many parties may be interested in gaining access to this information. Government agencies, for instance, might want to examine such data to investigate tax fraud or to monitor home energy consumption. Advertisers and marketers would find the information to be invaluable in planning commercial strategies.

As new services develop, not only will a single cable system carry a uniquely large share of personal information, but it also may play a role in providing the services that handle the information. For instance, cable companies themselves are already starting to offer security services; when they develop home banking, shopping, and other commercial services, the cable companies will be in a position to use the centralized subscriber information they are collecting.

Several safeguards have been suggested to protect cable subscribers' privacy. Some observers believe these safeguards can be enforced best through industry self-regulation. Warner-Amex recently took a step in this direction by adopting a privacy code that includes most of the specific safeguards discussed in the following paragraphs. There is little likelihood, however, that comprehensive Federal legislation embodying any of these protections will be adopted in the near future. Consequently, local governments may want to include them in franchise agreements or insure that they are included in individual subscription agreements.

One option is to require that each consumer, when executing the subscription agreement, be informed of and agree to any potential collection and release of information. The agreement could provide for the subscriber's right to renew this consent periodically and to require the operator to obtain additional consent if the system plans to act outside the parameters of the original agreement. In addition, the agreement should require subscriber consent before any data are monitored on an individual rather than a systemwide basis.

Officials may want to require cable operators to collect and maintain information in an aggregated way so that it cannot be broken down to reveal individual preferences or identities, and that any information collected on an individual basis, for billing or other purposes, be destroyed within a reasonable time. Officials may also want to insist that any individual information that is retained should be accessible to the individual, who will have the right to correct any errors and to be informed of any adverse effects, such as credit refusals, that are made on the basis of the information. In the event that provision is made for the transfer of information to government sources, local authorities may want to provide that such transfer take place only through a formal process that allows the individual an opportunity to be heard and that creates a record that permits subsequent verification that the government acted in a lawful manner.

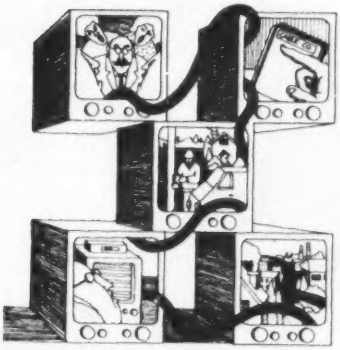
Local officials can make sure that cable operators are required to provide adequate security against unauthorized interception of information. The adequacy of security will vary with the design of each system, but the operator's plans should be detailed enough to allow careful review by interested officials and consumers.

Consumer Representation

Subscribers themselves may want to take an active role in monitoring consumer issues in cable service. One mechanism for providing consumer representation, adopted by many local governments, is a citizens' cable advisory board, appointed by the local government or elected by the system users themselves. To fund the board and make it more independent, some have suggested a voluntary check-off procedure whereby each subscriber indicates on the monthly bill that a part of the subscription fee paid should go to fund such a citizen board.

Another option for consumer representation in cable policy is consumer cooperative ownership of at least part of the cable system. Cooperative ownership can allow subscribers a more direct voice in the system's policies and procedures. Cooperative ownership is discussed more fully in chapter 6.

Appendix 1



Actors In The Industry

By

Joseph W. Waz, Jr.

Appendix 1: Actors in the Industry

Most of our Nation's telecommunications policy takes shape in the crucible of political debate in Washington, D.C. Congress sets the broad parameters of policy through the Communications Act of 1934, as amended. The task of administering the intent of Congress resides primarily in the Federal Communications Commission (FCC), an independent agency. It is in these two forums, Congress and the FCC, that representatives of the communications industry, State and local regulators, and public interest groups wage lobbying wars in an attempt to influence the directions of national policy. Although cable is essentially a local medium, its role in the Nation's telecommunications structure frequently makes it a center of controversy.

This appendix provides an introduction to the relevant Congressional committees and the FCC and to some of the more notable players among the many interest groups concerned with national policy on cable. The positions of these various organizations on some of the major public policy and legal issues concerning cable are also reviewed in brief.

Congress of the United States

House of Representatives
House Subcommittee on Telecommunications, Consumer Protection, and Finance
Rep. Timothy E. Wirth (D-CO), Chairman
Room B-331
Rayburn House Office Bldg.
Washington, DC 20515
Telephone: (202) 225-9304

U.S. Senate
Senate Subcommittee on Communications
Sen. Barry Goldwater (R-AZ), Chairman
Room 130
Russell Senate Office Bldg.
Washington, DC 20510
Telephone: (202) 224-8144

The House subcommittee is associated with the full Committee on Energy and Commerce, chaired by Rep. John D. Dingell (D-MI). The Senate subcommittee is associated with the full Committee on Commerce, chaired by Sen. Bob Packwood (R-OR).

The subcommittees are the first point of referral for bills introduced in the chamber that pertain to electronic communications.

Both houses of Congress have been engaged in an effort to rewrite substantial portions of the Communications Act of 1934 since the mid-1970's. The thrust of the legislation has been deregulatory; however, the political complexities of communications issues have effectively stifled all rewrite efforts to date.

Cable has been an infrequent subject of rewrite efforts. Of particular note are efforts in recent sessions of the Senate to pass legislation that would effectively preempt the authority of State and local bodies to regulate cable rates or to require the allocation of access channels. Vigorous lobbying has resulted in the defeat of such legislation. As this volume went to press, a new Senate bill (S. 2172) that would establish certain rules for cable television had been introduced to the Senate Subcommittee on Communications.

In the House, some attention has been paid to the difficulties of the cable franchising

process. In the 97th Congress, the House subcommittee has held hearings on franchising, and its staff is collecting information from more than a hundred municipalities and special interest groups on how franchising has proceeded. There is no indication that the House intends to intervene in the process; rather, it has characterized its role as providing a "clearinghouse" for the debate.

Federal Communications Commission (FCC)
1919 M St., N.W.
Washington, DC 20554
Telephone: (202) 632-7000

Cable Television Bureau
2025 M St., N.W., 6th floor
Washington, DC 20036
Telephone: (202) 632-6408
Contact: Consumers Affairs and Information Division

The FCC is the regulatory body empowered by Congress to regulate all interstate electronic communications. The Commission has exercised jurisdiction of one form or another over cable television since the 1950's. The extent of FCC regulation of cable crested with the adoption of extensive rules in 1972, but the Commission has gradually withdrawn from cable regulation, ceding this authority to State and local governments.

The Commission currently has in place restrictions on television/cable cross-ownership within a given market and limitations on ownership of cable systems by the major television networks and by telephone companies. A staff report prepared by the FCC's Office of Plans and Policy in 1981 recommended that the Commission eliminate many of its current ownership restrictions and consider no new ones.

The FCC has preempted local cable regulators from setting rates for pay cable programming; rate regulation is allowed only for basic cable services. The Commission has pending before it a rulemaking that would eliminate the current ceiling on franchise fees.

The current Commission chairman, Mark Fowler, has embarked on an effort to "unregulate" communications, removing government involvement in the "marketplace" to the greatest extent possible. Chairman Fowler has expressed support for removal of most ownership limitations concerning cable and other electronic media.

The Cable Television Industry

National Cable Television Association (NCTA)
1724 Massachusetts Ave., N.W.
Washington, DC 20036
Telephone: (202) 457-7600
Contact: Director, Public Affairs

NCTA is the largest cable trade association in the Nation, representing 1,800 systems, almost 300 associate members (equipment and program suppliers), and more than 350 other companies and firms. NCTA provides media services and research (surveys and reference reports), scientific and technological assistance, and publications to its members. It also is involved in government relations on both the Federal and State levels.

NCTA believes that cities have expanded their role as regulators beyond the proper scope. NCTA opposes rate regulation, finding that cable is neither a monopoly service nor an essential public utility. NCTA opposes municipal or not-for-profit ownership of cable, claiming that the private sector is better suited to provide responsive services, and arguing against governmental control of cable as improper under the First Amendment.

NCTA is generally concerned with any infringement on cable operators' First Amendment rights to exercise editorial judgment and control. The association argues that these First Amendment rights extend to all channels on the system. NCTA opposes federally mandated access and claims that access requirements written into local franchise agreements are improper and may be ignored by operators because they violate the First Amendment.

In opposing virtually all regulation of cable, NCTA points to the "double layer" of regulation the service now faces: Federally imposed content regulation applicable to locally originated cable programming, and State and local regulation requiring access allocations.

Community Antenna Television Association (CATA)
National Headquarters:
Ben V. Wiley, President
4209 N.W. 23rd St.
Suite 106
Oklahoma City, OK 73107
Telephone: (405) 947-7664

Washington Headquarters:
Steven Effros, Executive Director
3977 Chain Bridge Road
Fairfax, VA 22030
Telephone: (703) 691-8875

CATA is a trade association primarily representing about 650 independent, small cable system owners. CATA believes ownership and control of cable systems should remain with private enterprise. However, CATA has suggested that phone companies should be allowed to own cable only where a private party might not be willing to undertake it. CATA argues that rate regulation by localities has been used as a political tool and enforcement mechanism rather than for consumer protection, but agrees that rate regulation may on occasion be necessary, for example, for leased channel access. CATA does not oppose allocations for access if a system has sufficient channel capacity and in fact favors creating opportunities for leased access.

CATA cites First Amendment difficulties with government ownership or control of cable, and similarly notes serious First Amendment questions concerning what is in effect "government" control of local access channels. Unlike its big brother, NCTA, however, CATA believes First Amendment rights belong with the party that provides the programming; therefore, access channels are appropriately the province of the user, not the system operator.

CATA believes interconnection of systems is an economic question. If interconnection is not economically feasible, its cost becomes a regressive tax on poor and fixed-income subscribers. CATA also finds privacy to be an overblown issue in the cable context and believes that determinations of what information should be protected should be made for *all* related industries based on the content of the information, not the particular technology.

Related Industries (Broadcasting, Newspapers, Telephone)

American Newspaper Publishers Association (ANPA)
P.O. Box 17407
Dulles International Airport
Washington, DC 20041
Telephone: (703) 620-9500
Contact: Director, Telecommunications Affairs

ANPA is a trade association of approximately 1,400 member newspapers representing more than 90 percent of U.S. daily circulation. Members include dailies, nondailies, and newspapers published in Canada and elsewhere in the Western Hemisphere, both group owned and independent. ANPA's telecommunications department advises member newspapers on the opportunities and impact of new telecommunications technologies. The government and legal affairs office of ANPA is the organization's lobbying arm.

ANPA burst on the scene in the cable controversy during 1980, when proposed rewrites of the Communications Act were perceived as opening the door for American Telephone and Telegraph (AT&T) to become a significant force in "electronic publishing." ANPA strongly opposed granting telephone "common carriers" any editorial discretion in the transmission of

text services, and it lobbied effectively to limit the types of information origination that the legislation would allow the phone company to get into.

Because ANPA's member newspapers are also interested in electronic publishing via cable, the organization has taken a strong position favoring leased access availability on cable systems. ANPA has opposed efforts by certain cable system operators to withhold the leasing option.

American Telephone & Telegraph Co. (AT&T)
1000 Connecticut Avenue, N.W.
Washington, DC 20036
Telephone: (202) 457-3937
Contact: Division Manager, Media Relations

AT&T, the world's largest company, provides telephone service to 80 percent of all American residences. AT&T is not engaged in the provision of cable television services (under the ban on telephone/cable cross-ownership imposed by the FCC) although it has made a handful of tentative proposals to uncabled cities that it be allowed to build systems to be operated as common carriers; these proposals have never been pursued.

Because it has not engaged in the provision of cable services and its interests have not been directly affected by cable policy issues, AT&T has few organizational positions on cable. In debates in the Senate, over the deregulation of AT&T's Bell Telephone services, significant issues concerning the regulatory authority of local governments over cable became a bone of contention, but AT&T steered clear of the argument.

The divestiture by AT&T of its local operating companies, under a proposed settlement of a major antitrust suit reached with the U.S. Department of Justice in 1982, raises new questions concerning AT&T's future role in cable. This matter is likely to become the subject of congressional debate and public comment in the settlement proceedings.

Significantly, AT&T has been the center of controversy in the area of "electronic publishing," that is, wireline, electronically generated text services. AT&T has several such experiments in progress. Lobbyists for the newspaper industry (ANPA) have been AT&T's chief antagonists in arguments about the types of information AT&T would provide as an "electronic publisher" and who would exercise editorial control over the content.

The Commercial Television Networks

American Broadcasting Companies, Inc. (ABC)
1330 Avenue of the Americas
New York, NY 10019
Telephone: (212) 887-7777

CBS, Inc. (CBS)
51 West 52nd St.
New York, NY 10019
Telephone: (212) 975-4321

National Broadcasting Co. (NBC)
30 Rockefeller Plaza
New York, NY 10020
Telephone: (212) 664-4444

The three commercial television networks, in league with the broadcasting lobbyist organizations, actively opposed the introduction of cable television during the 1960's, calling it a threat to "free" (i.e., over-the-air, advertiser-supported) TV. However, CBS was among the earliest cable MSO's, and, in varying degrees, the networks are gradually making their peace with cable.

All three networks (in the case of NBC, its parent corporation, RCA) have moved into cable programming since 1980; CBS has initiated a cultural channel, ABC has begun cultural and women's channels and has news channels on the horizon, and RCA will premiere the

Entertainment Channel in 1982.

FCC ownership restrictions have kept the networks out of system ownership since 1970. However, the FCC granted CBS a request for partial waiver of its ownership ban in 1981, allowing CBS to build or obtain cable systems serving a very limited number of subscribers. CBS has since applied for the Alameda, California franchise, and has purchased a small cable system near Dallas, Texas.

Although the networks have not been involved in contests over control of cable content, they all have strongly opposed continued content regulation on broadcasters; all have sought repeal or modification of the Fairness Doctrine, equal time, and political broadcasting rules.

National Association of Broadcasters (NAB)
1771 N St., N.W.
Washington, DC 20036
Telephone: (202) 293-3500
Contact: Vincent T. Wasilewski, President

NAB is the largest broadcaster trade association, Its membership includes more than 4,700 radio and 660 television stations, including all the major networks. NAB is a service and lobbying organization, whose government relations department handles most of its work on Capitol Hill.

NAB led the opposition to cable in the early 1960's, claiming it would undercut the financial base of "free" (i.e., over-the-air, advertiser-supported) TV. In recent years, as broadcasting interests have also moved with greater frequency into cable ventures (within federally imposed restrictions), the NAB has restricted its face-off with cable to such issues as copyright liability for cable carriage of TV signals, and must carry status of certain TV signals and broadcast teletext.

Local Cable Regulators

International City Management Association (ICMA)
1120 G Street, N.W.
Washington, DC 20005
Telephone: (202) 626-4600
Contact: Assistant Director, Management Development Center

ICMA is a professional association for city managers, county managers, and directors of councils of governments. ICMA has 7,000 members worldwide. The organization provides training, education, and professional development services to its members.

ICMA does no lobbying and develops no organizational positions on issues such as cable. It does, however, facilitate the exchange of information between its members on cable franchising. ICMA anticipates launching a telecommunications committee in early 1982 that will examine how telecommunications can best be used for municipal services or programs.

National Association of Counties (NACO)
1735 New York Ave., N.W.
Washington, DC 20006
Telephone: (202) 783-5113
Contact: Director of Public Affairs

NACO is a membership organization representing county governments. Some 2,100 counties, representing urban, rural, and suburban America, are members. NACO provides research and technical assistance and actively lobbies.

NACO took a strong position in favor of county governments' right to regulate cable during Senate debates on the issue in 1981. NACO viewed the question of county regulatory authority as a "home rule" issue.

National League of Cities (NLC)
National Association of Telecommunications Officers and Advisors (NATOA)
1301 Pennsylvania Ave., N.W.
Washington, DC 20004
Telephone: (202) 626-3115
Contact: Director, Telecommunications Project

NLC is the oldest (founded 1924) and largest municipal organization in America, counting 800 cities and 48 State municipal leagues in its membership. NLC is a Washington advocate on behalf of cities before the Congress, the Executive Branch, Federal agencies, and Federal courts. One of NLC's five policy committees is devoted to transportation and communications issues; the policy committee drafts resolutions that, upon acceptance by the NLC members in convention, are published as "National Municipal Policy." NATOA, an organization of regulatory professionals from the State and local levels, is also affiliated with NLC.

NLC has expressed concern over legislative and judicial challenges to the authority of local governments to regulate cable. NLC supports retention by municipal governments of the authority to regulate rates for basic cable service. NLC seeks Federal laws granting local governments the exclusive authority to require the dedication of local, public, educational, governmental, and leased access channels. NLC has opposed concentration of control in media ownership as detrimental to the interest of local communities in responsive service. NLC also opposes Federal limits on franchise fees and welcomes, with reservations, ownership of cable systems by telephone cooperatives and independent telephone companies.

Public Interest and Consumer Organizations

Cable Television Information Center (CTIC)
1800 N. Kent Street, Suite 1007
Arlington, VA 22209
Telephone: (703) 528-6846
Contact: Director of Public Information

CTIC is a nonprofit membership organization for local governments that provides local governments an array of services related to cable television decisionmaking. CTIC has about 200 local government members. CTIC was started in 1972 with funding from the Ford Foundation and the John and Mary Markle Foundation, and since 1980 it has been self-supporting through its membership program.

CTIC monitors Federal and State legislation on cable television and works closely with other organizations to protect local regulatory control over cable. In its 11-year history, CTIC has helped more than 2,000 local governments with cable-related issues. It publishes several issue papers, books, and a monthly newsletter, *CTIC CableReports*, for local officials.

National Citizens Committee for Broadcasting (NCCB)
P.O. Box 12038
Washington, DC 20005
Telephone: (202) 462-2520
Contact: Executive Director

NCCB is a national nonprofit consumer organization chaired by Ralph Nader that is dedicated to protecting the public interest in electronic media. NCCB has 8,000 members nationwide and represents them in regulatory forums and before Congress. NCCB attempts to promote and enhance access to the media and protects consumer interests in radio and TV broadcasting, cable TV, and telephone services. NCCB cosponsored the first national conference; The Consumer and Cable TV in Washington, D.C. in 1981. It houses the Cooperative Communications Project, a public education and assistance effort promoting subscriber ownership of cable systems.

NCCB believes that effective regulation of cable on the local level requires active citizen involvement, either through direct ownership (the cooperative model) or through direct citizen

oversight (e.g., citizen committees on access and rate regulation). Because cable is essentially a local medium, NCCB observes, local ownership and control are central to responsive management. NCCB recommends the greatest possible separation of carrier (i.e., the mode of delivery) from content (i.e., programming) and strongly advocates maximum opportunities for leased, public, and other access programming. NCCB has opposed Federal efforts to diminish the regulatory authority of States and municipalities. NCCB has called for maximum efforts to protect subscriber privacy and has opposed concentration of media ownership by, inter alia, its intervention against two major cable-related mergers before the FCC.

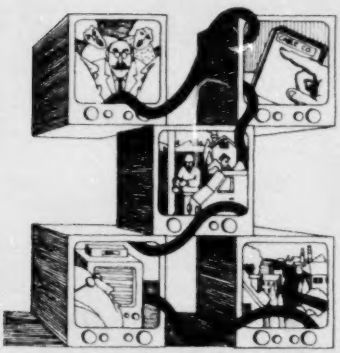
National Federation of Local Cable Programmers (NFLCP)
906 Pennsylvania Ave., S.E.
Washington, DC 20003
Telephone: (202) 544-7272
Contact: Executive Director

NFLCP was founded in 1977 to encourage use of cable access channels and to foster access to television. More than 3,000 individuals and organizations belong to NFLCP. Its membership includes cable access centers, libraries, educational institutions, independent producers, and interested individuals. The Advocacy Committee of NFLCP drafts resolutions for consideration by the organization's board, one of whose members is the committee chair. The NFLCP advocacy platform is then presented by the board to the delegates at the organization's annual convention for approval.

NFLCP believes that access to cable TV is based on the principle of freedom of speech and that each citizen's right to originate programming via cable supersedes any telecommunication enterprise's rights to originate programming. Because cable operates as a de facto monopoly in any given locale and marketplace forces are deficient in meeting the fullest range of community communication needs, government planning and regulation is necessary, NFLCP argues, and citizen participation in that planning is essential.

NFLCP argues that every person and organization must have the right to lease channel time and support services on cable systems for any legal use, whether sponsored or paid for by subscribers, without censorship or abridgment, on nondiscriminatory terms and at reasonable rates. NFLCP also advocates regulation to insure consumer privacy as cable provides an unprecedented array of consumer services, leading to accumulation of data on all facets of individual choice.

Appendix 2



Index of State Franchising Statutes

By

Sharon A. Briley

Appendix 2: Index of State Franchising Statutes

Alabama

Cities, towns, and counties are granted franchising authority by specific legislative acts. A local jurisdiction may not grant a franchise without obtaining specific legislative authorization.

Pending legislation (H. 63), introduced in January 1982, would empower county commissions to grant, by resolution or ordinance, franchises for the operation of community antenna television facilities, to condition such franchises on reasonable rules and regulations, and to levy and collect a license tax on the franchisees' gross revenues. The bill provides that existing operations would be grandfathered. Details of franchise regulation are not specified but left to county commission determination.

Alaska

The Alaska Public Utilities Commission, acting as the sole franchising and regulatory authority, requires all systems to obtain a certificate of public convenience and necessity. *Alaska Stat.* Sec. 42.05.

Arizona

The Board of Supervisors of a county or the governing body of an incorporated city or town has authority under State law to issue a nonexclusive license to cable television systems. The statute requires the franchise fee to be consistent with FCC regulations. *Ariz. Rev. Stat. Ann.* Secs. 9-505 through 9-508 (1974).

Arkansas

Municipalities, which have home rule powers under the State Constitution, have authority to grant franchises to public utilities. *Ark. Stat. Ann.* Sec. 73-208 (1947). The Arkansas Public Service Commission assesses cable television as a public utility for tax purposes only. *1974 Supp. Ark. Rev. Stat.* Secs. 84-103.1, 103.2, 103.3, Vol. 713.

California

Cities and counties may issue a franchise or license to cable television systems. *West Cal. Ann. Government Code* Sec. 53066. Cable television is excluded from the definition of public utility. While the PUC is given limited jurisdiction over the construction, operation, and maintenance of technical aspects of cable, for safety purposes, no regulations have been promulgated. *West Cal. Ann. Public Utilities Code* Secs. 215.5 and 768.5.

Franchising laws are under review, and a bill has been introduced (A.B. 2742) proposing comprehensive PUC regulation and preemption of local franchising. Other pending legislation includes bills to enforce the State deregulation law (A.B. 699, adopted in 1979), to extend the effectiveness of the same law beyond the present 1983 sunset, to revise the current theft of service law to deal with equipment distribution or manufacturing, and to limit foreign ownership.

Colorado

In addition to home rule powers, cities and towns are given statutory powers to license businesses, to grant public utility franchises, and to license and regulate the use of streets and sidewalks. *Colo. Rev. Stat. Ann.* Secs. 31-12-301, 31-15-301, 31-32-101, 31-12-101(b), and 31-12-101(20) (Cum. Supp. 1973). Counties may not grant franchises unless delegated such authority by statute; however, the Board of County Commissioners has control over rights-of-way. *Colo. Rev. Stat. Ann.* Sec. 30-11-107(1) (Cum. Supp. 1973).

The Judiciary Committee of the legislature is considering a bill (H.R. 1258) designed to protect local governments against potential antitrust liability.

Connecticut

The Public Utilities Control Authority, the sole franchising authority, issues certificates

of public convenience and necessity to cable companies, which are defined under State law as public utilities. *Conn. Gen. Stat. Rev.* Sec. 16-330-333.

Delaware

The Public Service Commission has statutory authority to grant franchises in unincorporated areas, to change or modify a municipal franchise, and to establish regulations for cable television. Municipalities are authorized to grant franchises within their incorporated areas. *Del. Code Ann.* Title 26. The PSC issues certificates for county areas, but it does not require a system to obtain a certificate if it has received a franchise from an incorporated municipality.

Florida

The State Constitution grants broad authority for municipal and county actions not otherwise prohibited by law. *Fla. Const.* art. 8, Secs. 1, 2. Municipalities have home rule powers. *Fla. Stat. Ann.* Sec. 166.021. Counties may grant an exclusive or nonexclusive license, in perpetuity or for a term of years, for the construction or operation of television lines along public streets. *Fla. Stat. Ann.* Sec. 125.42.

Georgia

Municipalities have authority to grant franchises under their home rule powers, although not specifically to cable television systems. *Ga. Code* Title 69 Sec. 310. Counties may grant one or more franchises to cable television systems and regulate by ordinance or resolution. Act No. 596, approved Apr. 9, 1981 (a. Laws 1981, p. 865).

Hawaii

The Division of Cable Television, a division under the Director of Regulatory Agencies, issues permits to cable television companies and has adopted comprehensive regulations. *Hawaii Rev. Stat.* Sec. 440G (1970).

Idaho

Cities have authority to franchise "utility transmission systems." A 1971 Idaho Supreme Court decision upheld the authority of municipalities to grant franchises to cable television systems. No specific authorization is contained in the statutes, nor are counties authorized to grant franchises.

Illinois

Municipalities have the express power to license, franchise, and tax community antenna television systems. *Ill. Rev. Stat.* ch. 24, Sec. 11-42-11 (1973). Municipalities include cities, villages, or incorporated towns but not townships. County Boards also may license, tax, or franchise community antenna television systems operating in unincorporated areas of the county. *Ill. Rev. Stat.* ch. 34, Sec. 429.24 (1975).

Indiana

Cities, towns, and counties have home rule powers. *Indiana Code,* Title 36. Counties are authorized to issue licenses, permits, or franchises for the use of county property. IC, Title 36, Sec. 36-2-2-23.

Iowa

Cities may grant, amend, extend, or renew franchises for cable television systems by ordinance after city election. *Iowa Code Ann.* Sec. 364.2 (1975). Counties are not empowered with home rule or franchising authority.

Kansas

Cities are authorized to grant franchises to cable television services. *Kan. Stat. Ann.* Sec. 12-2006 through Sec. 12-2014 (1974). Counties have home rule powers.

Kentucky

The State constitution confers broad franchising powers on cities, counties, towns, taxing districts, or other municipalities. *Constitution of Ky.*, Secs. 163, 164. No statute refers specifically to cable television.

Louisiana

Municipalities, including townships, may issue franchises. *La. Rev. Stat.* Sec. 33:4401. Parishes, i.e. counties, may also grant franchises. *La. Rev. Stat.* Sec. 33:1282 and *Constitution of La.*, 1921, art. 14, Sec. 3d. Police juries may grant franchises for the construction, maintenance, and operation of TV lines and cables. *La. Rev. Stat.* Sec. 33:4361.

Maine

Municipal officers may grant an exclusive franchise, not exceeding 10 years' duration. *Me. Rev. Stat. Ann.* Title 30, Sec. 2151, subsec. 2 (1974). Cable television is defined not to be a public utility (1974 law). Counties do not have franchising authority; however, few areas in the State are outside of municipalities.

Maryland

Municipalities may grant franchises under home rule powers. *Md. Ann. Code* art. 23A, Sec. 2(13). Commissioners of each county are authorized to grant franchises to community antenna television systems and to regulate rates and adopt rules and regulations for system operations outside of incorporated municipalities. *Md. Ann. Code* art. 25, Sec. 3C.

Massachusetts

Cities and towns have authority to issue nonexclusive licenses to cable television systems. *Mass. Gen. Laws Ann.* ch. 166A, Sec. 3 (West). The Massachusetts Cable Commission (MCC) sets licensing standards, and the licensing authority or the MCC may revoke a franchise. MGLA ch. 166A, Sec. 11.

Michigan

Cities, villages, and townships have home rule powers. *Mich. Comp. Laws Ann.* Sec. 117.1 *et seq.*; *Mich. Stat. Ann.* Sec. 5.2071 *et seq.* An opinion of the attorney general stated that all local jurisdictions in the State have the "right and obligation to regulate and franchise cable communications systems." Op. of the A.G. of Michigan No. 4808, Apr. 25, 1974. Counties have statutory and constitutional authority to permit the use of rights-of-way.

Minnesota

Municipalities are required to grant franchises to cable television systems. *Minn. Stat. Ann.* Sec. 238.08 (1974). Counties are included in the definition of municipalities. The Minnesota Cable Communications Board has adopted franchising standards and issues certificates of confirmation to cable systems.

Mississippi

A municipal charter of incorporation specifies powers of a particular municipality. No specific franchising authority for cable television systems is granted. Counties have no powers unless authorized by statute.

Missouri

Charter cities have franchising authority. *Mo. Rev. Stat.* Sec. 82.230. Home rule counties may grant franchises as provided by the State constitution (only two home rule counties). All noncharter cities, towns, villages, and counties are governed by statute which may or may not provide power to grant franchises.

Montana

Cities and towns may grant ordinances, franchises, and/or resolutions only for the right

to use or occupy the the public ways. *Mont. Rev. Codes Ann.* Secs. 11-1206 *et seq.*, 11-3126 and 11-3312 *et seq.* Counties do not have franchising powers.

Nebraska

Municipalities are empowered to grant franchises by ordinance to community antenna television services. They are also authorized to prescribe reasonable quality standards, regulate votes, and require extension of service. *Neb. Rev. Stat.* Sec. 23-383 through 388 *Reissue Rev. Stats. of Neb.* Sec. 18-2201 through 2205.

Nevada

The Nevada Public Service Commission issues certificates of public convenience and necessity to cable television systems, which are defined as public utilities. The PSC preempts local franchising authority. *Nev. Rev. Stat.* Secs. 711.010 through .180 and 37.010 (1967).

New Hampshire

Cities and towns are authorized to grant franchises for cable television systems, require fees, and impose conditions. *N.H. Rev. Stat. Ann.* Sec. 53-C:1. County authority is questionable.

New Jersey

A municipal consent by ordinance must be obtained from the municipal governing body to accompany application for a certificate of approval from the Board of Public Utilities. *N.J. Stat. Ann.* Sec. 48:5A-22. The Office of Cable Television within the Board administers the State's regulations.

New Mexico

Municipalities have authority to grant franchises under their home rule powers. *N.M. Const.* art. 10, Sec. 6. Counties have broad powers under State statutes. *N.M. Stat. Ann.* Sec. 15-36-1 *et seq.* Franchising of cable television is not included.

New York

Municipalities (including villages, towns, cities, and counties) may grant franchises to cable television systems. *N.Y. Exec. Law* Sec. 819 (McKinney). The State Commission on Cable Television issues certificates of confirmation and administers the many other regulations. *N.Y. Exec. Law* Sec. 811 *et seq.* (McKinney).

North Carolina

Municipalities are authorized to grant franchises to cable television systems. *N.C. Gen. Stat.* Secs. 160A-319 and 160A-311. Counties may grant franchises by ordinance to cable television systems. *N.C. Gen. Stat.* Sec. 153A-137.

North Dakota

Municipalities may grant franchises or privileges and may regulate their recipient. *N.D. Cent. Code* Sec. 40-05-01 subsec. 57. Some cities have franchising authority by virtue of their home rule powers. Counties do not have franchising powers.

Ohio

Municipal corporations and counties have franchising authority under their home rule powers to issue local ordinances. *Ohio Const.* art. 18, Sec. 3, *Ohio Rev. Code Ann.* Secs. 715, 717, 745.01 *et seq.* (municipalities); *Ohio Const.* art. 10, Sec. 3, and *Ohio Rev. Code Ann.* Sec. 301 *et seq.* (counties). Townships are authorized to enter into contracts with cable television companies to furnish cable service.

Oklahoma

Municipal corporations; i.e., cities, towns, and villages have authority to grant franchises. *Okla. Const.* art. 18, Secs. 5-7. Counties have no statutory authority to grant franchises.

Oregon

Home rule cities and counties have franchising authority, art. 11, Sec. 2 (cities), art. 6, Sec. 10 (counties). No specific cable television franchising authority exists.

Pennsylvania

Cities, townships, boroughs, and one town may issue permits to control rights-of-way for streets and roads. The extent of regulatory jurisdiction has been questionable for some time, however, particularly for second class townships and third class cities. Counties have no authority to issue permits.

Rhode Island

The Public Utility Commission, as the sole franchising authority, issues certificates to cable television companies. *R.I. Gen. Laws Ann.* Title 39, Sec. 19.

South Carolina

Municipalities have authority to grant franchises. *Const. of S.C.*, art. 8; *S.C. Code Ann.* Sec. 33-801. The governing bodies of municipalities and counties were granted specific authority to regulate the operation of any cable television system by State law enacted 6/29/76 (Act No. 688 of 1975).

South Dakota

Municipalities have exclusive jurisdiction by ordinance to regulate, prohibit, and consent to the construction, installation, operation, and maintenance of community antenna systems within their corporate limits. *S.D. Compiled Laws Ann.* Sec. 9-35-16 through 23 (1972). Counties have no franchising authority.

Tennessee

Municipalities and counties are empowered to franchise cable television companies and to regulate their operation. Ch. 334, 1977 Tenn. Public Acts.

Texas

All cities have franchising authority under home rule powers. *Vernon Ann. Texas Civil Stat.* arts. 961 through 1132, 1181, 1175, Sec. 12 (1973). Counties have no franchising authority provided by statute. The Public Utility Regulatory Act of Texas specifically exempted community antenna television services from regulation by the newly created Public Service Commission. *Texas Rev. Civil Stat.* art. 1446, Sec. 3(c)(2)(a).

Utah

Cities and towns have authority to adopt ordinances for public services. *Utah Code Ann.* Secs. 10-8-14, 15, 20, 21. The Board of County Commissioners may "grant franchises along and over the public highways . . . " *Utah Code Ann.* Sec. 17-5-39.

Vermont

The Public Service Board, as the sole franchising authority, issues a Certificate of Public Good on an annual basis and regulates cable television companies. *Vt. Stat. Ann.* Title 30, Secs. 501 through 507. Proposed legislation (S. 271) would authorize municipalities to grant, renew, amend, or rescind franchises and to collect reasonable franchise fees.

Virginia

Counties, cities, or towns may license, franchise, or issue certificates of public convenience and necessity to one or more community antenna television systems. *Va. Code Ann.* Secs. 15.1 to 23.1.

Washington

Cities, towns, and metropolitan municipal corporations have authority to grant franchises. *Wash. Rev. Code. Ann.* Sec. 35.27.330. Counties have authority to grant nonexclusive

franchises for rights-of-way. *Wash. Rev. Code Ann.* Secs. 36.55.010 and 36.55.060.

West Virginia

A municipality or a county commission is authorized to grant an exclusive or non-exclusive franchise to any person. *W. Va. Code Ann.* Sec. 8-31-1, 2.

Wisconsin

Cities and villages have home rule powers. *Const. of Wisc.*, art. 11, Sec. 3. Towns (three types) have no home rule and have only such powers specifically stated by statute. All land in the State is part of a village, town, or city.

Wyoming

Cities may grant franchises to "television companies." *Wyo. Stat. Ann.* Sec. 15.1-3, para. 31. No statute authorizes counties to grant franchises.